STAGGERS RAIL ACT OF 1980

HEARING

BEFORE THE

SUBCOMMITTEE ON SURFACE TRANSPORTATION

OF THE

COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION

UNITED STATES SENATE

NINETY-SEVENTH CONGRESS

FIRST SESSION

ON

OVERSIGHT OF STAGGERS RAIL ACT OF 1980

NOVEMBER 10, 1981

Serial No. 97–89

Printed for the use of the
Committee on Commerce, Science, and Transportation

U.S. GOVERNMENT PRINTING OFFICE
88-534 O WASHINGTON : 1982

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STAGGERS RAIL ACT OF 1980

TUESDAY, NOVEMBER 10, 1981

U.S. SENATE,
COMMITTEE ON COMMERCE, SCIENCE, AND TRANSPORTATION,
SUBCOMMITTEE ON SURFACE TRANSPORTATION,
Washington, D.C.

The subcommittee met at 9:30 a.m. in room 235 of the Russell Senate Office Building, Hon. John C. Danforth (chairman of the subcommittee) presiding.

OPENING STATEMENT BY SENATOR DANFORTH

Senator DANFORTH. This morning the Subcommittee on Surface Transportation will hear oversight testimony on the Staggers Rail Act of 1980. The witnesses will focus not only on the provisions of the act itself, but also on the Interstate Commerce Commission's implementation and interpretation of the provisions.

The basic goal of the Staggers Act is to improve the steadily declining economic health of the railroad industry by reducing the Interstate Commerce Commission's regulation of the industry. The act relies on competition, market demand, and creative pricing of services, instead of regulation, to establish reasonable rates and adequate service to shippers and to improve the financial viability of the industry. The act includes protections for shippers where there is no effective competition among carriers. The act contemplates that shippers will benefit from more reliable and improved service. The ability to enter into contracts allows shippers to take an active part in developing solutions to such concerns as rate stability and car supply.

We have a comprehensive list of witnesses today which includes representatives from the industry, Government groups, whose products move by rail, and groups who receive commodities by rail.

I would like to say to all witnesses and all in attendance that I have a problem this morning and the problem is this: There are 18 witnesses on the list, there are three rollcall votes scheduled this morning on the floor of the Senate, and it's going to be next to impossible to get through the list. The only way we can do it is to adhere to the short-time limitations. Each witness has been told the time limits. I want to assure you that without asking for it, the entire statement of each witness will be included in full in the record. Therefore, I ask that you take your allotted time to summarize your most pressing points. I am going to insist as the morning goes on that you stay within the prescribed time.

As our first witness today, we're honored to have Senator Quentin Burdick.

STATEMENT OF HON. QUENTIN BURDICK, U.S. SENATOR FROM NORTH DAKOTA, ACCOMPANIED BY COMMISSIONERS BRUCE HAGEN AND RICHARD ELKIN; AND JOHN FINSNESS, TRAFFIC DIRECTOR, NORTH DAKOTA PUBLIC SERVICE COMMISSION

Senator BURDICK. Mr. Chairman, thank you. I am pleased that the Senate Commerce Subcommittee on Surface Transportation is holding this oversight hearing on the Staggers Act. The Staggers Act is one of the more complex and far-reaching pieces of transportation legislation ever passed by Congress. Such drastic action was taken to deregulate the rail industry in order to improve its financial health, which in 1978 had a net rate of return on its investment of 1.62 percent.

The act allows rails greater freedom in setting rates, abandoning service, and offering different types of service such as contract rates to place it in a better position to compete with other producers of transportation, such as barges and trucks. I believe that it is extremely important for Congress to keep on top of the emerging trends as this country moves through deregulation of the rail industry.

The ICC's interpretation of the act must be reviewed as to what is and what is not permitted under the new economic regulatory environment, as well as the reaction of railroad management as to its newfound managerial discretion provided by the act.

One objection I have to the passage of the Staggers Act was that it decreased the time frame for the abandonment process. Deregulation has made it unrealistically simple for a railroad to abandon lines without concern for the impact on shippers, farmers, and small towns, which are dependent upon rail freight movement. Since passage of the Staggers Act the ICC has only denied 1 of 333 applications for abandonment. According to the Senate Appropriations Transportation Subcommittee report, North Dakota's major railroad lists 1,201 miles of its 2,221 branchline network as potentially subject to abandonment.

Publication of the required systems diagram map in North Dakota produced a strong public reaction against the railroad's plans. North Dakota's transportation system always has centered around its rail network. In fact, the framers of the 1889 North Dakota State constitution envisioned railroads as public highways, not roads. The expressed purpose of roads in North Dakota, as well as elsewhere, was to get the farmers out of the mud to reach a railroad station where adequate transportation existed for long hauls of freight or passengers. By 1916, there were 6,184 miles of tracks, and within a year few farmers were not more than 10 to 15 miles from a railhead.

Granted, a lot has changed since the advent of the railroad in my State—larger farms, development of a large road network, new grain marketing systems, all of which demand an update in our central railroad service network. North Dakota has already made considerable changes in adapting to these trends. The number of miles of track has declined from 6,184 in 1914 to approximately 4,900 miles. The railroads intend to ask us to scale back another 28 percent of our rail system. Such economic demands will adversely affect North Dakota, as well as neighboring farm States.

North Dakota has the distinction of not only being the largest wheat producer, but also having the largest freight bill in the country. Our grain producers, like so many others in rural, sparsely populated States, are captive shippers. We do not have reasonable alternatives to railroads for transporting of incoming and outgoing commodities. Rails are the most economical method of shipping, due to the vast distances, lack of water transportation, and the tremendous cost to improve roads to accommodate the shift of traffic from rails.

Under the Staggers Act the abandonment procedure must be completed within 330 days. That time frame even includes the whole appeal process. The public is given only 30 days from the date the application is filed to protest the railroad's action. If the application is not opposed within this 30-day period, the ICC must grant abandonment.

The filing of a protest does not guarantee that the ICC will conduct an investigation. The ICC's decision to investigate, which is wholly discretionary, is based on an analysis of the protest and written comments. Once the ICC has published its initial decision to grant abandonment, parties who wish to acquire or subsidize operations must file their offers of financial assistance within 10 days. This represents the public's final opportunity to preserve rail service. This time frame does not allow the general public much time to get together substantive comments protesting the application.

Second, if the ICC does investigate, it must render a decision within a tight statutory time frame. I am afraid that this will force the ICC to make decisions which are not carefully thought out and will have long-reaching consequences for the general public.

With me at the witness table this morning are two public service commissioners from North Dakota, Mr. Bruce Hagen and Mr. Richard Elkin. Also, the Commission's traffic director, Mr. John Finsness. They have prepared testimony for the committee's use, testimony on direct problems North Dakota has faced due to the passage of the Staggers Act.

I yield the rest of my time to Mr. Hagen.

Senator DANFORTH. Very good.

Mr. HAGEN. Senator, we believe that the oversight hearings on the Staggers Act should be continued for several years with yearly hearings by Congress. As we view it in a very real way, Congress said through the Staggers Act that the United States would have a private railroad system and that it would be profitable. What was left unsaid was who is going to pay for that system. In our view, and it shows in our testimony, our captive North Dakota shippers, farmers and grain elevators will be continued to require to pay more than they should pay for rail service.

The Staggers Act deregulates and removes from ICC jurisdiction all rail rates which provide revenues of less than 60 percent higher than variable costs. Similarly, market dominance findings of preferred jurisdiction in the Commission as to rate reasonableness on captive traffic, should it be determined solely on the same basis—that is, on rates which produce revenues greater than 60 percent of variable costs. Other criteria such as market share and geographical and product competition should be considered in the context of

reasonableness, but not in the context of the jurisdictional threshold issue.

Senator Burdick has covered abandonment. It's a very hot issue in North Dakota. We're very concerned about it. We're the State agency that does file to protest abandonment. We will be doing that in every instance to present the best case, but there is a shortage of time under the present law to properly prepare a case.

Additionally, we feel that book value, rather than current costs, should be attributed to cars and locomotives when arriving at the avoidable costs of branchlines. The criteria for market dominance and rate reasonableness findings and saving cost complaints should be the applicable criteria in place 180 days after October 1, 1980. We have a filing which we made within the 180 days under that act which shows that North Dakota farmers and producers are paying about $50 million more as of the time of filing on an annual basis to the railroads that serve North Dakota.

Revenue adequacy should be determined on the basis of imbedded debt rather than the current cost of capital, the latter representing windfall profits to the railroads. When implemented, intrastate rate regulation should be returned to the individual States subject to pre-Staggers Act standards. Further, we think Congress should investigate railroad holding companies. We believe our railroads should not be weakened now or in the future through any holding company device. We also believe that what properly belongs to the railroads should stay with the railroads.

Let me finish by just saying that we do want to have healthy railroads. We think effective regulation could help insure that fact. But with that, all we want is fair and equal treatment for the State of North Dakota.

[The statement follows:]

Statement of Bruce Hagen, Commissioner, North Dakota Public Service Commission

Mr. Chairman and members of the committee, my name is Bruce Hagen. I am an elected Commissioner of the Public Service Commission of the state of North Dakota and have held this post for the past twenty years during which time I have held the Transportation Portfolio. The laws of the state of North Dakota require the Commission to concern itself with interstate railroad rates, rules and practices to correct or prevent discriminations against its citizens. Commissioner Richard Elkin, President of the North Dakota Public Service Commission, and John Finsness, the Director of Traffic for our Commission, are with me today. Commissioner Elkin has served on our Commission for 15 years. John Finsness is an attorney and traffic and transportation expert with over 40 years experience and work in transportation. Commissioner Leo Reinbold the third member of our Commission is not able to be with us today but we fully concur in the unanimous statement we are presenting today to the Surface Transportation Subcommittee.

I want to express my appreciation to this committee for the opportunity to present our Commission's views on the implementation and effects of the Staggers Rail Act. Possibly the most important plea we can make is that further hearings of this type be continued in future years because we don't think that the effects of the Staggers Act on shippers or the railroads can be fully perceived in the short time span of one year. In addition, the one year of experience under the Act has been marked by a declining economy, slow grain sales because of unsatisfactory prices, and consequent huge surpluses of grain carrying hopper cars. In this connection we wish to state that North Dakota ships out as much as 450 million bushels of grain a year. While weights of different grains vary per bushel, based on 60 pounds per bushel of wheat, this figure translates into 135,000 hopper cars per year shipped. We also point out that the railroads have many locational monopolies in North Dakota—many towns, cities, and whole counties served by only one railroad.

North Dakota railroads have made a number of multiple car rate reductions on both east and westbound grain and some single car rates have also been reduced; we attribute these actions to competition from other producing areas served by other railroads, to truck competition and to the desire to utilize idle equipment. The strong efforts by the state of North Dakota through our Public Service Commission, our state Wheat Commission, our country elevators and other organizations and individuals, including our producers, also have helped to convince our railroads to make various rate adjustments. Other than the opportunity to take these actions on ten days notice as provided in the Staggers Act, rather than the former thirty days notice, we believe the carriers could have taken similar action under the previous law.

The development that concerns us most in North Dakota, a landlocked state heavily dependent upon rail transportation, is the Commission's current interpretation of the "market dominance" concept. This concept is, of course, the cornerstone of the remaining jurisdiction of the Commission in the area of the reasonableness of rates.

Basically the Commission's present stance discontinues the use of rebuttable presumptions in the determination of market dominance. Under the 4-R Act which was specifically not changed by the Staggers Act (Section 205(d)(3)(B)) the Commission issued rules declaring that a rebuttable presumption of market dominance exists if:

1. The rate in issue was discussed, considered or approved by rate bureau actions or
2. The proponent carrier handled 70 percent or more of the involved traffic or movement during the preceeding year or
3. The rate in issue exceeds the variable cost of providing the service by 60 percent or more or
4. Shippers or consignees have made a substantial investment in rail related equipment which prevents or makes impractical the use of another carrier or mode.

In spite of the fact that the law under the 4-R Act has not been changed, the Commission decided to discontinue the use of rebuttable presumptions in determination of market dominance and to rely on "general guidelines" embracing what is characterized as "the four major forms of competition" (Ex Parte 320 (Sub-No. 2)).

These are (1) intramodal competition (2) intermodal competition (3) geographic competition and (4) product competition.

Market dominance (49 USC 1070a) is defined as "the absence of effective competition from other carriers or modes of transportation for the transportation to which a rate applies". Consideration of geographic competition and product competition in market dominance determinations vastly expand the Congressional mandate in the preceeding sentence and, consequently, vastly reduce the Commission's jurisdiction having to do with rate reasonableness. If market dominance is not found because geographic or product competition exists, any issue with respect to rate reasonableness is terminated. The ICC is itself reducing its power to protect shippers from exploitation who otherwise have no reasonable alternative to rail transportation.

The market dominance concept and its legislative history is complicated. I do not have time in this short presentation to deal with it completely and recommend to this Committee's staff the ICC rationale (Ex Parte 320, Sub 2, July 7, 1981 and August 4, 1981 orders) and an exhaustive treatment by former Congressman Eckhardt published in the September-October, 1981 ICC Practioner's Journal.

Geographic competition as a regulator of rail rates on grain is, to us a farce if shippers are to be protected from exploitation; let me cite a few examples:

Winter wheat grown in Kansas and Nebraska is to some degree substitutable with spring wheat of which North Dakota produces the major supply. The Union Pacific (UP) has for years maintained lower rates, mileage considered, from Kansas and Nebraska to the North Pacific Coast for export than has the Burlington Northern from North Dakota to the same destinations.

While the Burlington Northern finally in 1980 made some supposedly competitive reductions, the end result was the following—the 50 car export wheat rate to the North Pacific Coast from North Platte, Nebraska on the UP is $1.68 per 100 pounds for a 1,490 mile haul while the BN rate from Jamestown, ND for a haul of 1,496 miles is $1.90. This is a difference of 22 cents per 100 pounds or 13 cents per bushel or $440 per carloads. Assuming BN and UP costs are comparable (and we believe that they are) and the UP knows what it is doing (which we believe is a reasonable assumption) we must speculate that the BN is engaging in exploitive behavior, The BN does, of course, compete more vigorously from its adjacent stations in Kansas and Nebraska. Wheat moving to Puget Sound for export has increased by 59.5 percent from the 1976–77 to the 1980–81 crop years. Of this, hard red spring wheat has increased 30.3 percent while hard red winter wheat has increased 69.7 percent.

There is truck competition on grain in varying degrees depending upon the length of haul from North Dakota to Minneapolis and Duluth, our principal markets. Assume the following: there is no truck competition; a not unlikely assumption in the near future; the UP sets rates from Kansas and Nebraska to these two markets, the BN in response meets the UP rates because of geographic competition. However, because from the same degree of longitude, the length of haul from Kansas and Nebraska will always be greater than from North Dakota, the BN will be able to meet the UP rate and pocket the difference between its shorter haul costs and the longer haul UP costs, again exploitive behavior. Thus, product and geographic competition will not serve to provide reasonable and nonexploitive rates. The market is not a substitute for regulation of a monopoly.

Product competition is another concept more complex than would first appear on the surface. Suppose three fourths of North Dakota farmers for one reason or another decide that they want a John Deere tractor. There may be other tractors made at other origins and even at better prices, but they want a John Deere. It is naive to think that the railroads are not able to recognize these differences in demand and not capitalize upon them.

The railroad pricing department has always been an unfriendly partner in the pricing decisions of grain producers as well as the pricing departments of manufacturers, but with one constraint—the law that every shipper be treated equally and fairly. The present course of the ICC is to allow the unfriendly railroad pricing department to participate more fully in the producers and manufacturers pricing department, to insert itself, if you will, into the nuances of demand pricing and to extract its share.

If the Commission removes itself from the fray—declares that market dominance does not exist because of geographical or product competition—the issue of exploitation will never arise.

The Commission in its August 4, 1981, order in Ex Parte 320 (Sub. No. 2) page 10, states that if petitioners are successful by administrative or judicial review in upsetting a Commission finding of the absence of market dominance, reparations will be available to make such petitioners whole. That is simply not the case with respect to grain. Farmers bring grain to local elevators in small trucks and are at least theoretically paid the market (Minneapolis) price less transportation and handling costs. This grain is commingled by the elevator, loaded into hopper cars, and sold at the Minneapolis price less transportation costs. The elevator shipper holds the freight bill and would be entitled to reparations. Elevators would be unable to prorate reparations back to the farmer who, while bearing the freight charges, did not actually pay them. The Commission has recognized this fact time and time again.

This whole fracas reminds me of the Canadian situation. As we understand it only two complaints attacking freight rates in Canada have been brought since regulation reforms were instituted ten years ago. The requirements to successfully pursue a rate complaint are so onerous that nobody brings a complaint. The government then says deregulation must be working, look, no one is complaining.

In summary, it is our opinion that the Commission's present guidelines to determine market dominance; intramodal competition, intermodal competition, geographic competition and product competition, are devices to allow the Commission to ignore the gut issues which are: what are the costs, what are the revenues, and what are the profits?

We venture to predict that determining the market dominance issue under present rules will require far more time on the part of the parties and the Commission than will the reasonableness issue—should a complainant get that far. The jurisdictional issue should rest solely on the now designated revenue-cost ratio.

ABANDONMENTS

North Dakotans are up in arms, to say the least, about Burlington Northern's announced plans concerning abandonments of rail line. The railroad's system diagram map indicated that out of 2,221 miles of branchline, in the state, 383 miles are in Category I and are potentially abandonable within three years. An additional 786 miles are designated as Category II and are under study for abandonment. These two categories in North Dakota involve at least twice as many miles as the same categories in any other state on the railroad's system.

The North Dakota Public Service Commission intends to contest these abandonment applications with all the resources at its command; however, if the Interstate Commerce Commission continues on its present course, success may be minimal. We say this because we understand that in the last twenty-five months the I.C.C. has

approved 330 abandonment applications out of 331 submitted. The one application denied is said to be the result of poor preparation on the part of the railroad.

This result lies more in the 4R Act of 1976 than in the Staggers Act although the latter did shorten the time frame for completion of abandonment applications. Some of these time frames are quite severe. For instance, while the railroad must advise the public of abandonment plans thirty days prior to the actual filing of the application, it is not until the application is filed that the public is advised as to the various financial details of the railroad's case. These figures must be analysed and challenged in and of themselves or by other evidence sufficient to convince the Commission that an investigation should be held. The protest must then be filed within thirty days of the filing of the application. The I.C.C. no longer must conduct an investigation although it currently appears to be doing so.

A complicating factor in the trial of abandonment cases is a court finding—*C & NW Transp. Co.* v. *U.S.,* 582 Fed. 2nd 1043, cert. denied, 439 U.S. 1039—that prior I.C.C. rules as to equipment costing methodology do not meet the requirements of the 4-R Act. In response to this decision the Commission is revising its rules to require the railroads to calculate equipment costs on the basis of the replacement cost for new equipment rather than on the basis of the value of the railroad's equipment as carried on the railroad's financial accounts.

This is apparently the state of the law, and it should be changed. The use of replacement cost for cars and locomotives rather that value as carried on the railroad's books in arriving at total avoidable (opportunity) cost places the railroad in a better and the protesting shipper in a worse position. Whether the intention of the 4-R Act was to bring this about or not, the purpose of this methodology is based on a fiction detrimental in no small way to abandonment decisions on marginal lines.

SAVINGS CLAUSE COMPLAINTS

In response to the Staggers Act, North Dakota filed nine complaints against eastbound and westbound grain rates. At the time of filing, we estimate that our North Dakota farmers paid $50 million annually in excess rates. In all some 850 complaints from across the United States have been filed under Sec. 229 of the Staggers Act constrictions providing that any rate not so challenged within 180 days were declared to be lawful.

Most of these complaints remain in limbo, embroiled in the railroads' attempt to revise cost update procedures within the Rail Form A Costing Formula and a court appeal of the Commission's addition of geographic and product competition criteria in its rules to determine market dominance. Administrative problems in progressing these complaints, alone, will serve to delay expeditious resolution of the complaints. Meanwhile, the basic market dominance threshold, the 1.60 revenue to variable cost criterion for 1980, has now increased to 1.65 and is programmed to increse to 1.80 by 1984. Basic questions arise. Will the commission assume jurisdiction at the threshold level applicable when the complaints were filed or when they are decided?

REVENUE ADEQUACY

The basic thrust of the Staggers Act is that railroads should earn adequate returns. It can be anticipated that the Commission will look first to this mandate. And they have with a vengeance. A revenue adequate railroad has now been declared to be a railroad which has revenues equal to the current cost of capital. By last report only three railroads in the United States meet this criterion. It is our thought that railroads earning revenues equal to embedded debt should be declared to be revenue adequate.

Given the above caveat as to revenue adequacy it can be anticipated that captive traffic such as grain, coal and chemicals will be required to furnish those revenues and to cross subsidize the less profitable traffic movements regardless of market dominance thresholds. Market dominance thresholds, whether a simple revenue/cost ratio or whether a complex mix of market share, geographic or product competitions, are no more than jurisdictional issues. The gut issue is the Commission's approach to and solution of the reasonableness issue. Again, it is too early to tell, and oversight hearings should be continued on a yearly basis.

INTRASTATE RATE JURISDICTION

The Staggers Act of pre-empted state jurisdiction on intrastate rates to the same extent as it pre-empted the jurisdiction of the Interstate Commerce Commission. Certification of states requesting such certification is not yet completed. Additionally, while it is clear that the states are subject to provisions of the Staggers Act, it is

not clear whether the states are also subject to the discretionary rules to be propounded by the I.C.C. by direction of the Staggers Act.

HOLDING COMPANIES

A study by the Commission directed under Sec. 903 of the 4-R Act entitled "Railroad Conglomerates and Other Corporate Structures" published on February 7, 1977, relates that presently the commission has declared that it has no jurisdiction as to the acquisition of control over more than one railroad when all the commonly controlled railroads are operated as part of a single system. The study also concludes that an equally plausible and supportable interpretation under Section 11343(a) could have been or could be that the Commission does have control over the formation of, in our case, the Burlington Northern Holding Company. While not specifically a Staggers Act legislative change, the asserted lack of jurisdiction in the Commission is of great concern to the state of North Dakota.

We believe Congress should investigate holding companies and the effects of separating land grant assets from the operating railroad in the light of the intent of the land grants. Those assets that belong to the railroad should stay with the railroad. Consideration should be given to land grant revenues in connection with railroad branchline abandonment applications.

Senator DANFORTH. Thank you very much, Senator Burdick and gentlemen, for your testimony.

The next witness is Robert W. Blanchette, Administrator of the Federal Railroad Administration.

STATEMENT OF ROBERT W. BLANCHETTE, ADMINISTRATOR, FEDERAL RAILROAD ADMINISTRATION

Mr. BLANCHETTE. Good morning, Mr. Chairman. I will try to help you with your timetable. I have found that on past occasions it's been in my own interest to be on and off quickly.

With your leave, Mr. Chairman, I'd like to have my written testimony lodged in the record.

Senator DANFORTH. You don't have to ask for leave because that will automatically be the case with all witnesses.

Mr. BLANCHETTE. In our testimony we note that it is obviously too early to make a complete assessment of the Staggers Act, but we do pass upon a few points. First, and I would like to reiterate it, we compliment the Interstate Commerce Commission for the speed with which it has addressed the problems raised by the act. It has done so in the past and continues to do so.

Second, we note the importance of the Staggers Act and the Northeast Rail Services Act remedies on the profitability of Conrail. I want to return to that point. Third, we note with considerable pleasure the way in which many railroads have addressed themselves to the contract rate provisions of the act. And finally, we comment with favor on the exemptions that are permitted on regulation.

If I leave nothing else with you, Mr. Chairman, it is the relationship between the Staggers Act and the Northeast Rail Services Act related to the profitability of Conrail during the great debate that raged in the early part of this year. All of Conrail's problems were thrashed out. Now, we noted that if Conrail was to remain a single entity, there were certain prerequisites and it was determined first, and you participated very heavily in these discussions and in the outcome, that Conrail would be weaned off the Federal dole and would be reintroduced into the private sector. In order to do that, certain very important things had to happen. Labor had to step up. It did. The commuter authorities had to step up. They will.

The linchpin, however, for the profitability of Conrail and for the end to its past history of subsidies is the ability of Conrail to take full advantage of the rate marketing and other freedoms which were introduced with the Staggers Act and with the Northeast Rail Services Act.

Conrail has reacted to that. Many of its measures have not been popular, as we said they would not be. I know, in my own home State of Connecticut, it has become a pilot program for the draconian remedies under the Staggers Act. But what we are doing there is working with the shippers, working with the local communities to see not how we can stifle the innovation and freedoms permitted to the act, but how we can accommodate and adjust to them. We're doing the same thing, for example, in South Dakota. We're doing the same thing in the Rock Island and Milwaukee territory.

Conrail views with concern many of the new winds that it sees blowing. I have no less concern. I would only note that if, in the case of Conrail and the railroads generally, they do not become attractive to capital investors, if they are not allowed to act like businesses, if they are put back into the iron maiden of regulation that choked the Penn Central to death, if they are fixed, for example, to a fully allocated cost standard of pricing and that is the maximum, if they are told that they must get away from differential pricing, then we are back to the subsidy, we are back to nationalization, we are back to the handouts. It is of critical importance to Conrail and to the American railroad industry that it be given the unfettered freedoms that everyone voted for and that the Congress enforced last fall.

[The statement follows:]

Statement of Robert W. Blanchette, Administrator, Federal Railroad Administration

Mr. Chairman and members of the Subcommittee, I appreciate this opportunity to comment on the Staggers Rail Act of 1980.

Although I believe that the changes we have seen thus far have been beneficial, I cannot advance a complete assessment on the effects of the Staggers Act. Together with the Railroad Revitalization and Regulatory Reform Act of 1976, the Staggers Act loosened regulation that had been in place for nearly a century. Many actions have been taken by the railroads, the ICC, and the shippers, actions which have had a significant impact on rail transportation in the United States. Nevertheless, the full impact of reduced economic regulation cannot be measured in only one or two years.

Several interim assessments can however, be made at this point. We do know, for example, that the flexibility afforded by the Act is essential to Conrail's survival. Further, the ability to enter into contracts has benefited railroads and shippers alike. In addition, the exemption of competitive traffic movements from regulation is increasing railroad participation in markets which had previously been dominated by motor carriers.

The Interstate Commerce Commission deserves much of the credit for the positive report I bring to you today. The ICC moved swiftly to implement the Staggers Act, issuing rules on most Staggers Act provisions within a few months of enactment. I agree with the ICC's interpretation on most of the issues and believe that the ICC has accurately reflected the intent of Congress. During the past year, the ICC has encouraged railroads to use the new freedoms of the Staggers Act; its decisions have, for the most part, supported those railroad industry initiatives.

The ICC's decisions on the major Staggers Act issues have reflected the realities of the marketplace in which the railroads must survive. The ICC has set broad guidelines for market dominance, indicating it is looking for realistic evidence of competition. In determining revenue adequacy, the ICC has recognized the nature of the capital markets in which the railroads must compete for funds. Following the legislative intent, the ICC has encouraged rail carriers and shippers to use contracts

for the broadest range of services and has carefully maintained the confidentiality of the contract terms.

CONRAIL

Under the Northeast Rail Service Act of 1981, Conrail must achieve profitability to assure its ultimate sale as a single entity. Without the flexibility of the Staggers Act provisions and the streamlined branchline abandonment provisions of NERSA, profitability is probably beyond Conrail's reach. In order to reduce the likelihood that Conrail will become a permanent ward of the Federal Government, we believe that the full range of marketing and pricing options provided by the Staggers Act must remain available to Conrail and that Conrail must aggressively employ these options.

Many of the actions which Conrail has taken and those it will be forced to take will result in increased costs to shippers, connecting railroads, or communities. There will be a temptation to restrict Conrail's latitude in applying the Staggers Act provisions. We must resist this temptation. If Conrail is prevented from using the marketing and pricing tools essential to its survival, we will incur a tremendous public cost to maintain rail service in the Northeast. If, however, Conrail is allowed to take reasonable advantage of the Staggers Act as part of its recovery plan, as anticipated by the NERSA legislation, then Conrail stands a chance of achieving profitability.

Many of Conrail's actions under the Staggers Act have been controversial. It is our conviction that the controversy results from the unprecedented nature of the actions and the swiftness with which Conrail took advantage of the Staggers Act, and not from any question of the validity or necessity of Conrail's implementing them. Conrail's principal Staggers Act actions have been:

Conrail implemented cost-recovery surcharges on traffic to or from 39 branchlines;

Conrail changed its grain rate structure, eliminating short hauls, inefficient routings, and transit privileges. This is under investigation by the ICC, but was not suspended;

Conrail canceled its participation in specific joint rates on grain. This action was suspended by the ICC pending the outcome of an investigation of the action;

Conrail established a new rate structure for nonferrous recyclables;

Conrail reduced backhaul rates on furniture and ferrous scrap to encourage increased car utilization; and

Conrail closed gateways with other railroads in situations where Conrail received only a short haul on the traffic. This is under investigation by the ICC, but was not suspended.

At FRA, we are dedicated to working with shippers and local communities in arriving at the requisite adjustments to some of these marketplace decisions. We are confident that an accommodation can be reached without resurrecting the Conrail subsidies of past years.

CONTRACTS

The statutory encouragement of contracts has had a beneficial effect on the quality of rail transportation. The railroads and their customers are creating imaginative and individually tailored solutions to problems that could not be solved by regulation. Innovative contractual solutions are being developed which embody new ways of addressing long-standing problems. Many contracts address the question of quality of service; including transit times, shippers' desires for high-value special equipment, shippers' interest in having a guaranteed car supply, the utilization of cars during periods of economic downturn, and rate stability. These contracts illustrate that creative and innovative solutions can be developed when people who have a problem are free to develop their own solution to that problem.

Contracting also eliminates much of the "red tape" that has long been a part of the railroad ratemaking process. Railroads and shippers are free to develop solutions to their problems without the anticipation of protests or unilateral investigations of the rate.

As railroad transportation moves into its less-regulated future, fixed-term contracts will become the shippers' principal means of assuring predictable rates and service levels for transportation needed months or years in the future. Contracts will also permit railroads to have a greater degree of confidence in future traffic projections and will give the railroads greater assurance that future traffic will be available to cover the costs of capital improvements necessary to handle the traffic.

Thus far, over 550 contracts have been executed by more than 50 railroads. Some railroads have been particularly aggressive in employing contracts as the basic class

of service in special situations. For example, the Missouri-Kansas-Texas and its subsidiary, the Oklahoma-Kansas-Texas, have entered into over 100 contracts. Many of these cover transportation to points on the former Rock Island main line operated by the OKT. Similarly, the LaSalle and Bureau County Railroad entered into contracts with each of the shippers on the segment of the Rock Island which it operated. In effect, the LS&BC became a "contract-only" carrier on that line segment, providing precisely the service the shipper desired.

The Illinois Central Gulf provides another example of a railroad which has implemented an aggressive marketing program incorporating contracts. The ICG has built a traffic "base" of transportation contracts which now total roughly four percent of the ICG's revenue dollars.

The contracts which railroads have entered into cover a wide range of rate and service considerations. While many are similar to existing annual volume tariffs, others reflect new ideas. They reflect the view of many shippers that service reliability, not price, is the most important consideration in purchasing transportation. They also reflect the carriers' desire to have predictable traffic levels, particularly when capital investments are necessary in order to serve the traffic. Some of the more innovative concepts incorporated in contracts include:

Guaranteed transit times with premium charges for good service and refunds to the shipper for service not meeting an agreed-upon standard;

Additional charges for guaranteed car supply;

Fixed rates that cannot be increased during the term of contract, even if general increases go into effect;

Payments to shippers for better utilization of cars;

Guaranteed train service to accommodate a shipper's volume on a daily basis;

Rate escalation agreements instead of periodic general increases;

Guaranteed turn-around time for shipper-owned cars;

Reduced rates on backhauls in trailers previously moved loaded in the opposite direction;

Additional charges and volume guarantees in exchange for purchase and installation of special railroad equipment;

Short-term demurrage relief on frozen export coal and substitution of other coal for export loading;

Shipments to be tendered in equal amounts during the term of the contract to avoid car supply problems;

Long-term annual volume requirements combined with shipper financial assistance to rehabilitate rail lines involved in the movement;

Reduced rates in times of car surplus on shipments in excess of average weekly traffic level; and

Various contract durations (3 months, 1 year, 15 months, 5 years, 20 years) to fit particular needs of individual carriers and shippers. Short term contracts (3 months) to utilize surplus cars.

The following table highlights some of the contracts which have unique features:

SAMPLE CONTRACT FEATURES

Railroad(s)	Commodity	Term	Special features
B. & O., 3 short lines	Coke	3 years	Minimum volume: 95 percent of consignor's rail shipments.
B.N.	Food products	1 year	Refunds for reloading cars destined to other BN stations; designed to meet trucks competition.
N. & W., B. & O.	Flour	2 years	Shippers cars, no transit or other usual privileges.
N. & W.	Coal	Up to 3 years	Implementing reservations to ease congestion at Lamberts Point coal piers (21 contracts).
MILW	Food products	3 months	Minimum of 200 cars per month; MILW penalized for insufficient car supply.
MP	Pulpboard	3 years	Decreasing rate, based on volume.
D. & R.G.W.	Motor vehicles	1 year	Shipper-carrier incentive payments to reduce empty mileage.
Southern	Grain	1 year	Shipper refunds for using surplus equipment over set weekly average.
C. & O.	Coal	10 years	Annual volume requirement, guaranteed car supply.
C. & O.	Auto parts	5 years	Volume incentive.

SAMPLE CONTRACT FEATURES—Continued

Railroad(s)	Commodity	Term	Special features
K.C.S.	Woodpulp, paper products.	20 years	Covers rates for hauling plus rental of tracks and yard facilities at shipper's mill.
N. & W.	Motor vehicles	5 years	Allowance to shipper based on loaded miles and allowance to N. & W. based on empty miles.
U.P.	Food stuffs	2 years	Assigned cars, annual volume requirement, service commitments.
La Salle and Bureau County	General commodities	1 year	Shipper pays a surcharge to established rate; carrier provides specified switching service, includes provision for track maintenance and rehabilitation.
G.T.W., B. & M., C.V., C.N.	Cornsyrup	5 years	Annual volume.
Va. & M.A.	Steel wire	6 months	Minimum 14 carloads per month; carrier pays $100 per car penalty if unable to supply.
MILW	TOFC	6 months	Shipper guarantees 1250 trailers; carrier guarantees at least 17 trains per week.
I.C.G.	Grain and feed	1 year	Rate varies with carrier turn-around time performance with shippers cars.
MILW	Clay	1 year	Small shipper contract for 5,000 or 10,000 ton per year movement.

EXEMPTION FROM REGULATION

The ICC's authority to exempt traffic or service from regulation was broadened by the Staggers Act, stimulating both intra- and intermodal competition. The recent exemption of piggyback traffic sparked keen intramodal competition for traffic out of Chicago to East Coast ports; Conrail has lowered its rates approximately 15 percent from Chicago to Philadelphia, New York, and Baltimore; the Chessie System has instituted a similar reduction; and the Norfolk and Western Railway has lowered its rates from Chicago to Norfolk and back.

Analysis of the experience with fresh fruits and vegetables, exempted from regulation in May, 1979, shows that rail market share can improve dramatically when rates are free to fluctuate according to demand. In 1980, the first full year after the exemption, rail car loadings of fresh fruits and vegetables showed a 38 percent increase over 1978, the last full year before exemption; tonnage increased 27 percent.

Rail's market share improved substantially for several commodities under the exemption. For example, the rail share of apple movements increased from 4 percent before the exemption to 14 percent in 1980, grapefruit increased from 19 percent to 28 percent, lettuce from 7.5 percent to 11 percent, and oranges from 24 percent to 37 percent.

Rail carriers are also making use of the exemption provision for other individual commodities. The CSX has petitioned for the exemption of citrus pomace and has begun to compete successfully in this truck-dominated Florida market. Conrail has petitioned the ICC to exempt traffic which moves in boxcars on the basis that this traffic is competitive with other transportation modes and does not need to be regulated.

INCREASED CAR UTILIZATION AND PRODUCTIVITY

The Staggers Act flexibility have enabled railroads to coordinate their rates with car supply and thereby get better car utilization. Through rate flexibility and contract rates, the rail industry has been able to increase productivity as illustrated by the following examples:

The Southern Railway is offering a rate discount on its surplus hopper cars;

The Burlington Northern Railroad has begun discounting its boxcars which are reloaded to BN stations in Chicago; previously, these were returned empty;

The Western Pacific Railroad and the Union Pacific Railroad are giving shipper allowances for the release of assigned cars;

The Norfolk and Western Railway coal contracts improve coordination with ocean carriers and reduce transshipment time; and

The Florida East Coast Railway provides discounts for use of underutilized enclosed multilevel cars.

SUMMARY

The Staggers Act has brought marketing into the forefront of railroad planning. Carriers are now allowed and even encouraged to contract with shippers and to tailor their services to the specific needs of shippers. Thus, a carrier can provide premium service in exchange for special rates or provide low priority service at any rate which contributes to the going concern value of the carrier.

With the tools provided by the Staggers Act and the Northeast Rail Service Act of 1981, rail carriers have the opportunity and ability to market their services aggressively and to prove themselves in a competitive environment. I am encouraged by the rail industry's response to date and I am confident the carriers will continue to utilize the Staggers Act to assure that railroads remain a competitive and profitable transportation mode.

Senator DANFORTH. Thank you, Mr. Blanchette.

The next witness is the Hon. Reese Taylor, Chairman of the Interstate Commerce Commission.

STATEMENT OF HON. REESE H. TAYLOR, JR., CHAIRMAN, INTERSTATE COMMERCE COMMISSION, ACCOMPANIED BY JANICE ROSENAK, LEGISLATIVE COUNSEL, AND WILLIAM SOUTHARD, DIRECTOR OF THE OFFICE OF POLICY AND ANALYSIS

Mr. TAYLOR. Good morning, Mr. Chairman. I have with me this morning on my right, Jan Rosenak, the Commission's Legislative Counsel, and on my left, Bill Southard, who is Director of our Office of Policy and Analysis.

I want to thank you for the opportunity to appear here today to present the views of the Commission with regard to the implementation and effects of the Staggers Rail Act of 1980. I have submitted a written statement for the record and would like to summarize that statement for you at this time. There is attached to the statement five appendixes, which I think summarize the Commission's actions with respect to the Staggers Act and what we have done to implement it.[1]

The Staggers Act significantly reformed Federal regulation of railroad transportation in an attempt to remedy the railroads' financial plight. The act was intended to assist the rail system to remain viable in the private sector, and to allow the railroads to compete more effectively between themselves and with other modes. To achieve this, the act modernized the regulation of railroads to place greater reliance on the marketplace and to remove unnecessary regulation. At the same time, it provided a regulatory process that balances the needs of carriers, shippers, and the public.

Given this overall mandate, the Commission in the last year has conducted numerous proceedings, many of which were specifically required by the new statutes. In implementing the act we have been cognizant of the increased emphasis on competition and on regulatory policy which would foster sound economic conditions in transportation, keeping in mind the goal of allowing efficient rail carriers to earn adequate revenues. We have attempted to balance the competing interests of all parties while complying with the letter and spirit of the Staggers Act.

[1] The material referred to has been retained in the Committee files.

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We believe that in general we have succeeded in this endeavor and that the result will be a more healthy, competitive industry with benefits accruing to all concerned. The Staggers Act and our implementation of the act has been successful, in our view, in removing unneeded regulatory burdens while retaining the protection afforded by regulation where there is an absense of effective competition.

While the full effects of the changes cannot easily be measured at this time, the legislation has had a significant impact. I am pleased to report that the Commission has moved forward expeditiously, despite the difficulty in simultaneously implementing both new rail and motor carrier legislation. Most of the key rulemakings have now been completed, so by the time of the next oversight hearings it should be possible to determine more definitively how well the policy goals of the Staggers Rail Act have been met.

Today, however, we can make some general observations on the effects of the act. Rail carriers' earnings have improved under the act. Data is available for the three quarters ending June 30, 1981, following the passage of the Staggers Act. During that period class I net railway operating income has risen 38 percent, compared to the same 9-month period of 1979–80. At the same time, railroad traffic increased by less than one-half of 1 percent. Since the traffic mix during this period has deteriorated due to economic conditions, and since we have no evidence that rail carriers are deferring maintenance, we believe that the carriers' increased earnings can be attributed in large part to the new provisions of the Staggers Act.

A second way to judge the impact of the legislation is by the extent to which its provisions have, in fact, been utilized. Unlike the period after enactment of the 4R Act, when little had happened 1 year later, there has been major activity in a number of areas under the Staggers Act. For example, more than 650 rail rate contracts have been filed with the Commission since the effective date of the act. We now receive about 100 new contract rate filings per month by rail carriers of all sizes involving a wide range of both shippers and commodities. The high number of filings indicates that both carriers and their customers see positive effects in the contract rate provisions of the Staggers Rail Act. We believe the contract provisions are among the most important in the act, and we predict that the filings will continue to increase as more railroads and shippers become aware that contracts offer answers to a wide variety of transportation problems.

There has also been considerable use by both large and small railroads of the joint rate surcharge and cancellation provisions of the act. Our preliminary estimate is that the surcharging railroads collected $10.2 million in revenues from the surcharges during the year. We estimate that only one-half of 1 percent of all shipments, however, are subject to this type of charge.

Another important Staggers Act change is the expansion of the Commission's exemption authority under 49 U.S.C. 10505. Since passage of the Staggers Act, the Commission has modified and streamlined its exemption procedures. We have finalized the exemption of TOFC/COFC traffic and now have under consideration a related exemption pertaining to trucking operations that are

railroad affiliated or controlled. According to reports that we have received, many rates are lower and service substantially improved as a result of the TOFC/COFC exemption.

Also, the Commission is actively considering exemptions in a number of other areas. The possible exemption of export coal traffic and light-density line abandonment has been proposed. Conrail has filed a petition seeking the exemption of boxcar traffic. Use of the exemption in the securities area to eliminate delays in bringing public offerings to market is being studied. Other candidates for exemption include trackage rights applications, or joint ownership or joint use agreements. Computer and other empirical research efforts are being utilized to study rail transportation of all commodities, to determine which rail services meet the statutory criteria for exemption.

My prepared statement summarizes many of the extensive rulemakings the Commission has conducted pursuant to the Staggers Act. While time does not permit a discussion of the individual proceedings at this time, suffice it to say that the proceedings have been many and complex, and overall I believe they have contributed toward accomplishing the goals of the Staggers Act.

In summary, the Commission is of the view that the Staggers Act is a sound and forward-looking law, and our experience with it has been generally favorable. To some degree, the effects of this law are not yet clear, with the result that, in most instances, legislative changes do not appear desirable until more experience has been gained.

The Staggers Act was a necessary response to a difficult and complex situation, and we have every reason to believe that it will be beneficial to both the rail industry and the public over the long run. Should problems of a serious nature become evident, we will of course bring them to the attention of Congress.

Thank you for this opportunity to comment. I would be pleased to try to answer any questions that you might have.

Senator DANFORTH. Mr. Taylor, I want to ask you about the proposed coal rate guidelines.

The position will be taken by Mr. Dempsey in his testimony that the proposed guidelines and their possible future progeny could bankrupt railroads. Mr. Dempsey is concerned that if the standard is applied to rates on other commodities as well as coal, the result could be annual railroad revenue losses of over a billion dollars. I have three questions relating to this:

First, has the Commission taken into account the possible financial impact of the guidelines for coal on the railroad industry?

Second, is the Commission reconsidering the wisdom of this proposal?

Third, if it is not, is it considering whether or not to apply guidelines to other commodities?

Mr. TAYLOR. Mr. Chairman, let me say that we too are very, very concerned about these coal rate guidelines. We've had—as I guess perhaps you know—historically some trouble with coal rates.

Ex Parte No. 347 (Sub. No. 1) is being reconsidered at this very moment. I am extremely hopeful that we will have something out by the end of the year. I spent the better part of a day a while back, sitting with our staff and talking about some new coal rate

guidelines, because we are all too well aware of their national impact on the industry. The proposition that we have suggested previously may not really be the best answer. As a consequence, the matter is under consideration by the Commission at the present time.

I really can't discuss the details of what the staff has proposed. It is under consideration. We hope to get something circulated for the rest of the Commissioners' review very shortly, and I would hope that we will have something out on this before the end of the year.

Senator DANFORTH. Thank you very much.

I also have a question from Senator Long: Do you feel that Congress should go ahead and fund the Railroad Accounting Principles Board?

Mr. TAYLOR. There is a portion of our lengthy statement which talks about that, under the heading: "Title III: Railroad Cost Determinations." I think the first paragraph really explains our position.

The bottom line is: No, I don't think we need it. I think we're able to function without it. I would simply state that it doesn't need to be funded. It hasn't been, and we see no necessity of its being. But if it is, we'll work with it.

[The statement follows:]

STATEMENT OF HON. REESE H. TAYLOR, JR., CHAIRMAN, INTERSTATE COMMERCE COMMISSION

Mr. Chairman and members of the subcommittee, I want to thank you for the opportunity to appear here today to present the views of the Commission with regard to the implementation and effects of the Staggers Rail Act of 1980. In addition to the following statement, we have included: (1) a table listing all Ex Parte proceedings conducted pursuant to the Act showing the status of the proceeding; (2) a brief summary of each Ex Parte proceeding; and (3) a brief summary and list of all litigation involving the Staggers Act. We have also attached a short list of various problems we have had in interpreting the Act and some suggestions for technical amendments to clarify the intent of Congress in these matters.*

INTRODUCTION

The Staggers Rail Act of 1980 significantly reformed Federal regulation of railroad transportation in an attempt to remedy the railroads' financial plight. The Act was intended to assist the rail system to remain viable in the private sector of the economy and to allow the railroads to compete more effectively among themselves and with other modes of transportation.[1] To this end, the Act modernized the eonomic regulation of railroads to place a greater reliance on the marketplace and to remove unnecessary regulation while providing a regulatory process that balances the needs of carriers, shippers, and the public. Given this overall mandate, the Commission in the last year has conducted numerous proceedings, many of which were specifically required by the new statute. In implementing the Act, we have been cognizant of the increased emphasis on competition and on regulatory policy which would foster sound economic conditions in transportation and allow efficient rail carriers to earn adequate revenues. We have attempted to balance the competing interests of all parties while complying with the letter and the spirit of the Staggers Act.

We believe that in general we have succeeded in this endeavor, and that the result (although it is still too early for definitive statements) will be a more healthy,

*Appendices I, II, III, and IV, respectively.

[1] The goals of the Act, as set forth in Section 3, are as follows: (1) to assist the railroads of the Nation in rehabilitating the rail system in order to meet the demands of interstate commerce and the national defense; (2) to reform Federal regulatory policy so as to preserve a safe, adequate, economical, efficient, and financially stable rail system; (3) to assist the rail system to remain viable in the private sector of the economy; (4) to provide a regulatory process that balances the needs of carriers, shippers, and the public; and (5) to assist in the rehabilitation and financing of the rail system.

competitive industry with benefits accruing to all concerned. The Staggers Act, and our implementation of the Act, has been successful, in our view, in removing unneeded regulatory burdens while retaining the protection afforded by regulation where there is an absence of effective competition. While the full effects of the changes cannot easily be measured at this time, the legislation has had a significant impact. I am pleased to report that the Commission has moved forward expeditiously, despite the difficulty in simultaneously implementing new rail and motor carrier legislation. Most of the key rulemakings have now been completed, so by the time of the next oversight hearings, it should be possible to determine more definitively how well the policy goals of the Staggers Rail Act have been met.

Today, however, we can make some general observations on the effects of the Act. Have rail carriers' earnings improved under the Act? We think so.

Data is available for three quarters since the passage of the Staggers Act. During that period, ending June 30, 1981, Class I net railway operating income has risen 38 percent to $1,215 million from $878 million in the same 1979–1980 nine-month period. Since railroad traffic increased by less than one-half of one percent (705 billion revenue ton miles vs. 702 billion revenue ton miles), three principal factors could be responsible for the increase in operating income: (1) Rates rising faster than costs. (2) Improved traffic mix. (3) A combination of the first two.

Our study indicates that the traffic mix has deteriorated as the result of the current recession. Movements of high-rated manufactured products, such as automobiles, are down from even the depressed levels of 1980. Lumber and wood product shipments have been adversely affected by the sharp decline in housing starts.

As to costs, we have no evidence that the railroads are deferring maintenance in order to report higher earnings. Maintenance expenses are the main area where the railroads can "manage" their income accounts. Maintenance levels, in real terms, have risen in recent years and as of yet we see no evidence of any sharp cutback although results vary from railroad to railroad. Should the recession deepen, we would expect to see maintenance levels decline.

This leaves higher rates as the main reason for the advance in rail earnings over the nine-month period ending June 30, 1981. While we cannot prove that this is due to the Staggers Act, our feeling is that the Act has succeeded in contributing to the improvement in rail earnings.

A second way to judge the impact of the Staggers Act is by how much its new provisions are utilized. Unlike the period after the Railroad Revitalization and Regulatory Reform Act of 1976 (4R Act) when little had happened one year later, there has been major activity in a number of areas under the Staggers Act. For example, more than 650 rail rate contracts have been filed with the Commission since the effective date of the Act. We now receive about 100 new contract rate filings per month by all sizes and types of rail carriers on a wide variety of commodities. The most active railroads in the contract rate area to date include the Missouri-Kansas-Texas, Southern Railway, the Chicago and North Western, the Milwaukee Road, Norfolk & Western, the Southern Pacific, Burlington Northern, Conrail, and the Atchison, Topeka, & Santa Fe Railway Company. The high number of filings indicates that both carriers and their customers see positive effects in the contract rate provisions of the Staggers Rail Act. We believe the contract provisions are among the most important in the Act, and we predict that the filings will continue to increase as more railroads and shippers become aware that contracts offer answers to a wide variety of transportation problems.

There has also been considerable use of the joint rate surcharge and cancellation provisions of the Act. During the past year, 113 surcharges became effective, 67 of which were filed by Conrail. Included in the 113 surcharges were 37 applying to traffic over light-density lines. It should also be noted that 10 Class III rail carriers filed 27 of the 113 surcharges. Our preliminary estimate is that the surcharging railroads collected $10.2 million in revenues from the surcharges during the year. While the level of activity has been high in this area, we would stress that relatively few shipments are subject to this type of charge. We estimate that only one-half of one percent of all carloads are subject to surcharges. A list of surcharge filings is included in Appendix V.

Another important Staggers Act change is the expansion of the Commission's exemption authority under 49 U.S.C. § 10505. The Commission can now use its exemption authority whenever its regulation is unnecessary to effectuate the rail transportation policy of section 10101a and either (1) the transaction or service is of limited scope or (2) regulation is not necessary to protect shippers from the abuse of market power. The amendment was clearly intended to broaden the Commission's exemption powers.

Since passage of the Staggers Act, the Commission has modified and streamlined its exemption procedures. We have finalized the exemption of TOFC/COFC traffic

and proposed, further, related exemption of certain railroad operations in the trucking area. The TOFC/COFC exemption has been affirmed in all significant respects by the Court of Appeals for the Fifth Circuit. According to reports we have received, many rates on fruits and vegetables are lower and service has substantially improved.

The Commission is actively considering exemptions in a number of other areas. Possible exemption of export coal traffic and light-density line abandonments has been proposed. Conrail has filed a petition seeking exemption of boxcar traffic. Use of the exemption in the securities area to eliminate delays in bringing a public offering to market is being studied. Another candidate for exemption is trackage rights applications or joint ownership or joint use agreements under 49 U.S.C. 11343(a)(6). As a practical matter, these transactions are rarely opposed (except by labor, which we would proposed would still receive the standard protective conditions) and are routinely approved. Computer and other empirical research efforts are being utilized to study rail transportation of all commodities, to determine which rail services meet the statutory criteria for exemption.

I would like to turn now to a discussion of particular provisions of the Act and the Commission's implementing decisions.

Title-by-Title Analysis of the Implementation and Effects of the Staggers Act

TITLE II—RAILROAD RATES AND INTER-CARRIER PRACTICES

This title provides the railroads with substantially more rate freedom than was afforded prior to the Staggers Act. Generally, in the absence of market dominance, a rail carrier may establish a rate at any level it desires (absent discrimination) so long as it contributes to going concern value. The title also establishes a revenue-variable cost threshold below which the Commission has no jurisdiction over the reasonableness of rates. If the carrier has market dominance and the rate exceeds the jurisdictional threshold, the Commission must determine whether or not the rate is reasonable.

In determining whether a rate is reasonable, the Commission is required to recognize the policy that rail carriers are to earn adequate revenues. Basically, this title eliminates rate regulation where there is effective competition. It also encourages carriers to use new marketing techniques by permitting contracts, permissive limited liability rates, entertainment expenses, and premium charges to encourage better car utilization. Surcharges are permitted without the concurrence of other parties to the joint rate to assure that carriers may earn revenues of 110 percent of variable costs or close routes not providing this level of earnings.[2]

Provisions in this title also simplify coordination, minor merger procedures, entry, and reciprocal switching agreements. Finally, title II encourages the Commission to utilize its expanded exemption authority so as to regulate only where necesssary to protect against abuses of market power.

In order to implement this title, the Commission conducted over 30 Ex Parte proceedings. An attachment to this statement provides a brief summary of all of these proceedings. At this point we would like to discuss some of the more far-reaching and pivotal of these decisions, as well as those Committee staff indicated were of special interest.

Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations and Considerations of Product Competition

Accurate market dominance determinations are central to fulfilling the goals of the Staggers Act, namely, that competition and demand for services are to be the determining factor in railroad rates except where there is an absence of effective competition.

Ex Parte No. 320 (Sub-No. 2) reflects the provisions of the Staggers Act and our experience to date with the market dominance rules established pursuant to the 4R Act. Basically, the proceeding had two purposes: (1) the reexamination of existing market dominance regulations; and (2) a determination, as mandated by section 205 of the Staggers Act, whether and to what extent "product competition" should be considered in determining the reasonableness of rates.

Our decision in this proceeding eliminates the prior rebuttable presumptions of market dominance based on cost, market share, and substantial investment. The presumptions have been replaced with general guidelines. Because of the wide

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[2] Except for light density lines, the authority to establish surcharges expires in 1983 unless extended for one additional year by the Commission.

variation in circumstances from case to case, we believe the flexible approach we have adopted will provide a more useful and reliable method for determining the railroads's market power in a given situation.

With regard to product and geographic competition, we concluded that these factors should not be considered in our reasonableness determinations. Since such assessments are based primarily on a comparison of the challenged rate and the cost of a movement, consideration of product competition (which has little, if any, bearing on costs) would provide no additional insight. Moreover, product competition would be difficult to quantify in this context. In our view, the concept is more relevant as an evidentiary tool to be used, as we have in the past, in determining whether a carrier is market dominant vis-a-vis particular traffic.[3]

Ex Parte No. 399, Cost Recovery Percentage

Section 202 of the Staggers Act required the Commission to calculate, within six months of passage of the Act and annually thereafter, the cost recovery percentage (CRP) for all rail traffic. The Act defined the CRP as that ratio of revenue to variable cost which, if all rates above it were deemed to have produced only revenues resulting in the cost recovery percentage, would, in the aggregate, when combined with total revenues from other traffic, provide revenues sufficient to cover industry-wide variable plus fixed costs (including a return to equity and debt, calculated at the embedded debt level). The CRP would not have an actual regulatory use until October 1, 1983 if the CRP is less than 175 percent or October 1, 1984 if it is above that level, at which time it becomes the threshold revenue/variable cost level for assertion of Commission jurisdiction over rail rates. The statute further prescribes that in no event can the CRP be less than 170 percent or more than 180 percent.

For purposes of meeting the six-month statutory deadline, the Commission decided to use the Rail Form A costing methodology to set the initial CRP level. Before October 1, 1983 (the earliest date on which the CRP could become effective), the Commission decision can be revised to reflect changes and improvements in costing techniques, such as adoption of a new Uniform Rail Costing Methodology, now being considered by the Commission.

The Commission decision was issued on April 1, 1981 and set the CRP at 197.5 percent. Since the statute prohibits it from being set higher than 180 percent, it would, if actually in effect, be set at that level. The decision explained in some detail how the figure was derived, and noted that it reflected a large volume of traffic now moving at rates below variable cost. With passage of the Staggers Act and changes in joint rate procedures and minimum rate standards, the decision expressed the view that there will be less traffic moving below variable cost, and that the CRP will be correspondingly lowered.

Ex Parte No. 393, Standards for Railroad Revenue Adequacy

The Staggers Act and the legislative history emphasize the railroads' need for adequate revenues to rehabilitate the rail system in order to meet the demands of interstate commerce. While the statutory definition of revenue adequacy was not changed,[4] the Act directed the Commission to conclude an adequate revenue proceeding within 180 days and to determine which rail carriers are earning adequate revenues within the same 180-day period and on an annual basis thereafter.

In Ex Parte No. 393, mandated by section 205 of the Act, the Commission determined that a railroad will be considered revenue adequate if it has a rate of return equal to the current cost of capital. In assessing the value of a railroad's investment base for the initial determination of revenue adequacy, the Commission used the sum of the original cost of track assets, betterments to track, and the depreciated book value of all other assets. The investment base was not adjusted to reflect special tax provisions such as accelerated depreciation and investment tax credits. The cost of capital was calculated using the current cost of debt and equity for the rail industry, and a debt-equity ratio of 40:60. This calculation results in a cost of capital of 11.7 percent, based on 1979 data.

In this proceeding, the Commission repealed earlier standards and procedures which had established a range of revenue adequacy, with the high value measured by the cost of capital and the low value based on a funds flow analysis. In revising the standards, the Commission pointed out that the low level calculation using funds flow analysis was never intended as a long term level of adequate revenue.

[3] Under our prior regulations, product and market competition were not considered germane in computing market share, but such evidence could be introduced to show that effective competition existed.

[4] See section 10704(a)(2).

The Commission also noted that the prior standards were inappropriate in view of the Staggers Act provisions limiting rail pricing flexibility under various sections for rail carriers earning adequate revenues.[5]

In its decision, the Commission indicated that a new proceeding would be opened to consider whether to use replacement (rather than historical) cost in calculating the investment base, and whether the appropriate revenue adequacy measure is the railroad's own (rather than an industry-wide) cost of capital.

Ex Parte No. 290 (Sub-No. 2), Railroad Cost Recovery Procedures

This proceeding implemented section 203 of the Staggers Act; the section provides that the Commission shall publish a "rail cost adjustment factor" at least quarterly as a basis for a zone of rate freedom to compensate the railroads for cost increases due to inflation. The Commission's decision adopted as the most acceptable measure of changes in rail costs the input price index compiled by the Association of American Railroads, as supplemented by the Producer Price Index for those costs not covered by the AAR Index, corrected and modified by the Commission as necessary. The ICC rules, based on forecasted increases in expenses, replace prior general increase procedures and authorize inflation-based increases without regulatory delay. Various parties contended that the AAR index, which is an index of the costs of railroad transportation inputs, necessarily overstates the increase in the cost of producing railroad outputs (transportation services) to the extent productivity increases occur. The Rail Act does not specify whether an input cost index or an output cost index is to be used as the rail cost adjustment factor. The Commission concluded that an adjustment to reflect productivity gains was not warranted at this time while the rail industry is earning inadequate revenues. The Commission will continue to study possible alternatives to the index, including development of an ICC composite index, and to make revisions and modifications as appropriate. The index procedures are available for collective adjustment of rates until at least April 1, 1982.

Ex Parte No. 387, Railroad Transportation Contracts

As previously indicated, there has been substantial use of the contract provision, section 208 of the Staggers Act. Proposed implementing rules have been issued in Ex Parte No. 387. We have attempted to devise workable rules that will encourage the filing of contracts—without impairing the rights of protestants. While the proposed rules were to become effective on an interim basis, those rules were stayed by the Commission following institution of a court action. However, the record in this proceeding is now complete and a decision will be issed shortly. In the meantime, we have been evaluating contracts on a case-by-case basis.

A Contract Advisory Service has been established within the Commission to provide advice to interested parties and to disseminate the summaries of contract filings; the Service appears to be functioning smoothly. It has met with hundreds of shippers and the officials of most major railroads. The mailing list developed by the Contract Advisory Service includes over 2,200 interested shippers and carriers, all of whom receive non-confidential contract summaries and other information in accordance with section 208 of the Act. In appropriate instances, the Commission has used its exemption power to shorten the notice period for contract filings.

Ex Parte No. 388, State Intrastate Rail Rate Authority

Under section 214 (new section 11501(b)), we have an affirmative obligation to certify a State authority once we determine that the standards and procedures submitted by the State are in accordance with Federal law. The Commission instituted this proceeding to review filings by State authorities seeking certification. These filings were reviewed and found not to contain information in sufficient detail to justify the requisite statutory findings. We then issued a subsequent notice indicating our concern, seeking more information, and provisionally certifying all 40 States which had applied.[6] We are now in the process of reviewing additional submissions filed by 36 States.

During this time we have received and timely acted upon a significant number of requests for relief by rail carriers under § 11501(c) alleging that actions of certain States were not in accordance with the statute. As the Commission stated in Ex Parte No. 388, every effort will be made to assist the States in meeting their responsibilities under the new law.

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[5] See, for example, section 203, Zone of Rate Flexibility. Section 217 of the Act also provides greater freedom in applying surcharges for carriers not earning adequate revenues.

[6] The States that did not request certification, and those which have not refiled under our order, have lost jurisdiction to regulate intrastate rail transportation.

Ex Parte No. 411, Complaints Filed Under Section 229 of the Staggers Rail Act of 1980

The rate freedom provided by the Staggers Rail Act begins with a rate level known as the "base rate." In general, the base rate is the rate in existence on October 1, 1980. However, the Act provides an exception: complaints alleging that existing rates are unreasonably high may be filed within 180 days from the effective date under section 229. During that period, which expired on March 30, 1981, 864 complaints were filed.

In an attempt to organize the processing of this tremendous number of complaints, we developed procedures for their handling which are different from those typically used. First, we required the railroads to file answers to them and urged both sides to submit joint responses. We specifically requested information with regard to whether settlement was contemplated, whether the Commission's offices would be useful in bringing about settlement, whether oral hearing, cross-examination, or other procedural tools would be necessary in particular cases, and whether certain proceedings could and should be consolidated. Second, we announced our intention to handle in two stages those cases that did proceed to formal adjudication. The first stage would address solely the issue of market dominance in order that time and expense would not be devoted to developing evidence that would not be used because we did not have jurisdiction to review the rate. If market dominance is established, the Commission would then proceed to the second stage to take evidence and analyze the reasonableness of the challenged rate. In response to our request, the parties have filed numerous pleadings.

On October 29, 1981, the Commission's Chief Administrative Law Judge held a docket management conference to refine further the procedures for handling these complaints. A substantial number of the complaints have been settled or dismissed. As to the remaining complaints, numbering 737 at this time, a report detailing the plan for processing will be issued by the Administrative Law Judge within the next several days. The Commission is optimistic that pending settlement negotiations will be successful in many instances, and that the final number which must be processed will be considerably lower than 737.

Ex Parte No. 403, Rail Carrier Cargo Liability Study

Section 211(d) of the Staggers Act required the Interstate Commerce Commission to recommend to Congress within one year of enactment whether rail carriers should continue to be subject to 49 U.S.C. section 11707. That section codifies the common law governing carrier cargo liability, providing a uniform strict liability standard for railroads and other transportation companies.

The Commission's report to Congress did not recommend that rail carriers be exempted from section 11707. With respect to specific issues raised by section 211(d), the Commission recommended that the Interstate Commerce Act be amended to: (1) eliminate the venue restrictions of the Staggers Act; (2) provide the courts with authority to award attorney's fees to successful claimants; and (3) remove the $10,000 jurisdictional threshold for access to Federal courts. The Commission decided not to recommend: (1) exemption of non-market dominant traffic from section 11707; (2) imposition of a comparative negligence standard; (3) imposition of a no-fault standard; (4) changes in applicable substantive laws; (5) changes in time limits; or (6) statutory provisions governing special or consequential damages. The Commission pointed out, however, that in the absence of market dominance, the only effect of requiring full liability rates may be the publication of excessively high rates in those cases where rail carriers choose to limit their liability through released rates.

The report was sent to Congress and made available to the public on September 30, 1981.

Ex Parte No. 282 (Sub-No. 7), Special Intermodal Authority

This proceeding implements new section 11344(e) which was added by section 228 of the Staggers Act. This section permits a rail carrier or its affiliate, together with affected shippers, to file an application for motor carrier service prior or subsequent to rail transportation where rail service by other railroads is inadequate. Interim rules were adopted and proposed as final.

Few comments to the notice were received, and no applications have been filed under the interim rules. This provision may be less important now that we have exempted from regulation TOFC and COFC movements by railroad companies in Ex Parte 230 (Sub-No. 5).

Ex Parte No. 282 (Sub-No. 3) and (Sub-No. 8), Railroad Consolidation Procedures and Railroad Consolidation Procedures Time Revisions

These proceedings revise procedural and informational requirements and the time limits for applications by rail carriers under 49 U.S.C. §§ 11343–11346. The revised procedures affect rail mergers, consolidations, acquisitions of control, purchases, leases, contracts to operate property of a carrier and trackage right agreements.

In September, 1980, in Ex Parte No. 282 (Sub-No. 3), the Commission adopted changes to its procedural regulations that had been proposed for comment the preceding November, and published proposed informational regulations. Several months later, in Ex Parte No. 282 (Sub-No. 8), the Commission proposed (and made effective on an interim basis) changes to the time limits applicable to rail consolidation proceedings to implement section 228 of the Staggers Act.

The regulatory changes in Ex Parte No. 282 (Sub-No. 3) were developed primarily to ensure that the amount and kinds of information required in an application will vary in accordance with the significance of the transaction involved. Informational requirements have been reduced for some transactions. Other transactions subject to our jurisdiction have been deemed to have no regulatory significance and have been exempted from the Commission's regulation.

Other revisions, for the most part technical in nature, have been proposed in response to comments received from concerned parties. Such changes are aimed primarily at clarifying the regulations and streamlining various stages of these proceedings.

Ex Parte No. 282 (Sub-No. 6), Railroad Consolidation Procedures, General Policy Statement

This proceeding is a revision of the Commission's policy statement governing rail consolidations. Between the time when the first Notice was published and the final regulation was adopted Congress enacted the Staggers Act. As a result of that action the Commission revised its notice in two ways.

First, the policy statement was limited to cases involving the merger or control of at least two Class I railroads. This was necessary because of the change in section 11344 setting different criteria for other rail consolidations.

Second, the Staggers Act added a new statutory criteria for mergers involving two Class I railroads. The Commission was explicitly required to consider the effect on intramodal competition.

In general the policy statement discusses the importance of rail consolidations in furthering national policy to rationalize the Nation's rail facilities and reduce excess capacity. It explains the statutory factors the Commission must examine as well as the balancing test employed in determining whether the transaction is in the public interest. It also discusses Commission policy on: conditioning consolidations; inclusion of other carriers; labor protection; cumulative impacts and crossover effects; and public participation.

TITLE III—RAILROAD COST DETERMINATIONS

This title provides for the creation of a Railroad Accounting Principles Board to establish principles for determining economically accurate railroad costs directly and indirectly associated with a particular movement of goods. The Board is to establish these principles within two years of enactment of the Staggers Act. Once established, the Commission is to promulgate rules to implement and enforce them. To date, this Board has not been funded. Also, the Report of the House Committee on Appropriations on the 1982 Legislative Branch Appropriations Bill, Report No. 97–170, to accompany H.R. 4120 (P.L. No. 97–51), at page 37, after recommending no funding for the Board, states that the Commission's new accounting system should be given the opportunity to achieve the necessary objectives before initiating another effort which may create confusion and redundancy.

This title also requires a preliminary and final certification by the Commission of rail carriers' cost accounting systems.

In this same general area, I would like to mention that the Uniform Rail Costing System (URCS) has been completed and is now being commented on by railroads, shippers and the public in general. As you are aware, this sytem has been under development for some time and the railroad industry, shippers and general public have been kept informed and invited to give views on changes and improvements. Thus far, we have every reason to believe URCS is a vast improvement over Rail Form A, the rail costing methodology used over the last 40 years. We have yet to finally conclude that the regression formulas which determine railroad variability are the ones that should be used. We are waiting for public comment on these. Presently, we contemplate implementing URCS by the early Spring of 1982.

TITLE IV—RAILROAD MODERNIZATION ASSISTANCE

This title establishes a new feeder railroad development program which gives shippers and interested persons (other than Class I or II railroads) the opportunity to acquire a rail line carrying less than 3,000,000 gross ton-miles of traffic per mile in the preceding year if the railroad is not providing adequate service. Three years after enactment, any rail line may be acquired under this provision. The Commission may require a carrier to sell a line to a financially responsbile person if the public convenience and necessity requires the sale or if the line is listed on the carrier's system diagram maps in category 1 or as potentially subject to abandonment under category 2.[7]

The Commission implemented this provision in Ex Parte No. 395, Feeder Railroad Development Program. Our rules require offerors to submit evidence that they are capable of paying the constitutional minimum value of the line and of providing adequate service for 3 years. The rules are designed to encourage privately-negotiated agreements. We will set the value only if the parties fail to agree. We are currently processing two competing applications, and several notices of intent to file feeder applications have also been received.

Title IV also establishes new time limits for considering abandonment applications and discontinuance of service. Applications for abandonments which are not opposed are to be granted within 45 days. For applications which are opposed, the Commission must process and decide the case within nine months. The Commission implemented this provision in Ex Parte No. 274 (Sub-No. 6), Abandonments of Rail Lines and Discontinuance of Service. The most significant changes caused by these rules are in: (1) the time frames governing the processing of abandonment and discontinuance applications; (2) the elimination of the automatic right to appeal initial decisions; and (3) the procedures for making offers of financial assistance either to subsidize continued operations or to purchase the rail line being abandoned.

Concerning appellate procedures, the final rules interpreted section 10904(c)(3) to allow an opportunity for appeal from an initial decision in an abandonment proceeding only where an investigation has been conducted. In those cases, it is a matter of Commission discretion whether an appeal will be heard. Although there is no opportunity to appeal from decisions in protested but not-investigated proceedings, the final rules allow parties to petition to reopen these proceedings after issuance of the administratively final decision. Finally, since the amended statute requires the Commission to grant all unprotested abandonments, there is no provision for administrative review of decisions in these proceedings. In the event of procedural defects (such as the loss of a protest in the mail, timely filed protests not coming to the attention of the decisional body, the failure of the applicant to afford the public the requisite notice of its proposed abandonment, etc.) the Commission will entertain petitions to vacate certificates issued in nonprotested proceedings.

In the financial assistance area, the final rules detail the procedures for filing offers. Moreover, the rules describe the mechanism which allows the parties to request the Commission to intercede and establish the conditions and amount of compensation for subsidy or purchase of the line.

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[7] We should note that the Northeast Rail Service Act of 1981 (NERSA) could have a substantial adverse impact on the feeder line program. Because the listing of lines on a system diagram map is no longer a prerequisite to Conrail abandonments pursuant to NERSA, Conrail has withdrawn its map. This precludes future feeder line applications for Conrail lines unless applicants can meet the more difficult public convenience and necessity criteria of section 10910(c)(1).

Most of the interest which has been expressed in using the feeder line program has been directed at Conrail lines. Therefore, these changes will probably affect the use of this program substantially.

We note also, however, that lines for which Conrail files abandonment applications may still be acquired by others through offers of financial assistance under section 10905 because the provisions of NERSA direct offerors to use the procedures under 10905(d)–(f). One potential problem here is that Conrail could seek such high divisions with potential purchasers of Conrail lines under section 10905 that these purchases will never be consummated. A possible solution for this would be to amend 49 U.S.C. 10905(3) to include language tracking either the language used in connection with discount purchases of Conrail property under section 1156(a) of NERSA (section 308(e)(3)(A) of the 3R Act) or that found in section 10910(f) of the feeder line program.

One other aspect of section 10905 that may require clarification is whether labor protection is required to be imposed if a line subject to abandonment is purchased under this section. The present section 10905 seems to leave a gap in labor protection for lines acquired under that section. If this "gap" is not intentional, language similar to that found in section 10910(j) could be added as section 10905(g).

TITLE V—CONRAIL TITLE V LABOR PROTECTION

This title modifies the labor protection provided to Conrail employees. The Commission was not required to implement or oversee its provisions, and thus will not comment on the title. We would note, however, that new Conrail labor protection provisions have since been enacted in the Northeast Rail Service Act of 1981.

TITLE VI—EXPEDITED SUPPLEMENTAL TRANSACTION PROPOSALS

This title required the Secretary of DOT, within 240 days after the effective date of the Staggers Act, to determine whether to propose a supplemental transaction for the transfer of all rail properties of Conrail in Connecticut and Rhode Island to another carrier in the region. If he had so proposed, USRA, the Commission, and the subject States were to comment on the proposal. No such proposal was submitted by the Secretary, and the section has been replaced by a new Connecticut-Rhode Island provision in the recent Conrail legislation.

TITLE VII—MISCELLANEOUS PROVISIONS

The only provision of this title particularly relevant to Commission actions deals with the Alaska Railroad. The Commission was required, within six months of enactment of the Staggers Act, to complete a study to determine whether certain rail-water contract rates of the Alaska Railroad would, if such rates were entered into after enactment of the Staggers Act, have violated section 10701a(c)(1) of title 49, United States Code, as amended by the Act. That section specifies that a rate cannot be considered to be below a minimum reasonable level if it contributes to going concern value; rates that equal or exceed variable cost (defined to include only those costs varying directly with the level of service), are conclusively presumed to contribute to going concern value.

The study, conducted by the Bureau of Accounts in Ex Parte No. 405, Alaska Rail Rate Study, found the contract rates to be well above the minimum reasonable level. The study required the Commission to examine several different cost levels because of peculiarities of the Alaska Railroad's cost center accounting system and allocation of the fiscal year 1980 Alaska Railroad capital subsidy. The minimum level was approximated by excluding capital costs and certain overhead; rates on the traffic at issue on average were 245 percent of that level and 175 percent of a "direct cost level" which would include allocable capital subsidy and would approximate Rail Form A variable costs. A subsequent study for a Congressional Appropriations Committee found the Alaska Railroad's rail-water traffic in general (of which the contract rate traffic is only a part) to be profitable, although not as profitable as the traffic considered in Ex Parte No. 405.

SUMMARY

The Commission is of the view that the Staggers Act is a sound and forward-looking law, and that our experience with it has been generally favorable. To some degree the effects of this law are not yet clear, and in most instances legislative changes do not appear desirable until more experience has been gained. The Staggers Act overall was a necessary response to a difficult and complex situation, and we have every reason to believe that it will be beneficial both to the rail industry and the public over the long run. Should problems of a serious nature later become evident, we will of course recommend further change.

Thank you for this opportunity to comment. I will be pleased to respond to any questions you may have.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR LONG AND THE ANSWERS THERETO

Question 1. Shortly after passage of the Staggers Act, members of the ICC and other highly placed staff members publicly stated that shippers should conduct their business as if the ICC did not exist. Does that represent your philosophy and that of the present members of the Commission?

Answer. If such statements were made, they do not reflect my view, nor do I believe they reflect the philosophy of the Commission. I have personally made quite clear—both at my confirmation hearing and subsequently—my view that the Commission is bound to implement fully the laws it administers in conformity with the express provisions of such legislation and the intent of Congress. In the rail area, we

are guided by the rail transportation policy and the goals and findings of the Staggers Act. The Commission is required to balance the needs of disparate interests and is receptive to and carefully considers all views presented in any proceeding.

Question 2. Under the Staggers Act when the railroad is market dominant the shipper is entitled to a reasonable rate. Where the railroad is not market dominant the shipper has no such right. Do you believe this unequal treatment is fair when railroads in many instances are able to charge extremely high rates even though they are found technically, not to be market dominant? Should not all shippers be entitled to reasonable rates?

Answer. All shippers should be entitled to reasonable rates. Under the present statutory scheme, the Commission is authorized to determine reasonableness where there is market dominance while competition is presumed to ensure reasonable rates in other instances.

The question you raise relates to the Commission's rate jurisdiction. The legislative history of the Staggers Act and the new rail policy adopted in that legislation stressed the railroads' need for additional revenues and a policy of allowing "to the maximum extent possible, competition and the demand for services to establish reasonable rates for transportation by rail."

The specific provision governing standards for rail rates (49 U.S.C. § 10701a) limits the ICC's jurisdiction to instances where the rail carrier has market dominance over the transportation. In enacting the Staggers Act and the Railroad Revitalization and Regulatory Reform Act of 1976, Congress determined that competition would ensure a reasonable rate structure where market dominance did not exist. The Commission's authority is of course limited to exercise of the jurisdiction granted by Congress.

Question 3. Title 49 U.S.C. § 10701a(b)(1) provides that if a rail carrier has market dominance over the transportation to which a particular rate applies, the rate must be just and reasonable.

(a) In how many cases during the last year where contracts were not involved has the Commission found existing rates to be in excess of reasonable rates? Please identify.

(b) Do you think there is any such thing as a captive shipper?

(c) If so, how do you identify them?

(d) Assuming that market dominance has been established, the Commission seems to have discarded every test of reasonable rates used in the past. How would you define an "unreasonable rate" today?

Answer:

(a) Unfortunately, the Commission does not keep records in a form that indicates which decisions found existing rates to be in excess of reasonable rates. As a general matter, relatively few rail rate decisions involving reasonableness have been decided by the Commission in the last year. This is because the notice of proposed rulemaking in Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines—Nationwide, and passage of the Staggers Act compelled reopening of the records in various major cases, and final decisions have not yet been issued. In addition, cases filed under the Savings Provision, section 229, are still pending. Thus, although we cannot provide you with actual figures, there have probably been few cases during the past year in which the Commmission found existing rates to be in excess of maximum reasonableness.

(b) and (c) Yes, captive shippers do exist. The Commission, in Ex Parte No. 320 (Sub-No. 2) Market Dominance Determinations and Consideration of Product Competition, 365 I.C.C. 118, established detailed guidelines for determining if a shipper is "captive." In essence, a captive shipper is defined as one over which a railroad has sufficient market power to exercise monopoly pricing. When a queston arises as to whether a shipper is "captive," the Act requires the shipper to establish that alternative transportation is unavailable or, if available, that the cost of it is impracticably high. Once the shipper has made a showing of market dominance the rail carrier has the burden of establishing an affirmative defense that: (1) the involved rate is below the Commission's jurisdictional threshold; or (2) that product or geographic competition or other factors exist which rebut the showing of market dominance.

(d) The Commission has endeavored to establish guidelines for maximum reasonable rates. Needless to say, this is a very difficult issue in view of the need to balance the shippers' right to service at reasonable cost, the carriers' need for adequate revenues, the public interest in a stable rate structure and national energy goals. In a recent decision in Ex Parte No. 347 (Sub-No. 1), Coal Rate Guidelines—Nationwide, the Commission: (1) determined that the development of an appropriate maximum rate methodology required further analysis; (2) sought additional comments from the parties; and (3) indicated that, in the interim, a case-by-case analysis would be used in determining maximum reasonableness. Thus, the

Commission presently determines whether a rate is reasonable based on the evidence introduced in an individual proceeding. We are continuing to analyze the information we have received in Ex Parte No. 347 (Sub-No. 1), and it is our expectation that maximum rate guidelines for coal and other commodities will be established in the near future.

Question 4. A lot of observers are of the opinion that to determine market dominance on the assumption that geographic and product competition are relevant elements is going to require a full-fledged antitrust-type hearing. Do you agree? If so, do you think such a test meets the requirements of the 4-R Act (Sec. 202(b)) that the Commission establish rules, standards, and procedures for determining market dominance so that there can be "a practical determination without administrative delay" of that question? Is not the Commission's handling of the complaints under section 229 of the Staggers Act, or lack of such handling, proof that the Commission has not met that requirement? Can market dominance be determined without administrative delay and the Commission's present interpretation of the statute?

Answer. Although determining the issues of product and geographic competition involves analyses somewhat similar to that used in antitrust cases, a full-fledged antitrust hearing is not necessary. Even though the analysis may be similar, it need not take a protracted amount of time to conduct. We believe we can make the requisit determinations within the statutorily mandated time frames and without administrative delay. For example, in a recent case (No. 38566, Rates on Iron Ore to Escanaba, MI, Chicago and Northwestern), the Commission analyzed the evidence in the record on product and geographic competition within the eight-month statutory deadline. It was concluded that, in spite of the rail carrier's extensive presentation with regard to alleged competitive alternatives, market dominance existed.

It should be noted that proof of product or geographic competition is essentially an affirmative defense. The shipper does not initially have to prove the absence of it. Rather, the carrier first must make a prima facie case that such competition exists. Only then does the shipper have to introduce evidence attempting to show that there is in reality no effective competition. Thus, it is entirely possible that the issues of product and geographic competition might not even be raised in a particular proceeding, thereby facilitating the fulfillment of the Commission's obligation to make a determination without administrative delay. We are firmly convinced that market dominance, as presently interpreted by the Commission, can be determined without administrative delay.

With regard to the section 229 cases, it is true that there have been some delays. However, we do not believe this demonstrates that consideration of competitive issues unduly delays decisions. These cases represent a unique situation which the Commisssion has attempted to handle through new techniques. Rather than assuming a role as merely an arbiter between disputing parties, we have attempted to encourage and assist in voluntary settlements. We have been quite successful in this attempt—from an original list of more than 800 separate proceedings, several hundred have been voluntarily settled.

We should also note that both complainants and defendants in these proceedings have raised many new and complex issues of statutory interpretation and policy. Understandably, the parties have been hesitant to proceed expeditiously until these issues have been decided. There have been large numbers of procedural and substantive motions which must be acted upon by the Commission, and which have had the effect of somewhat delaying the process. Nonetheless, as mentioned, we believe this is due to the unique situation involved in the savings provision cases and does not reflect a pattern of administrative delay.

Question 5. Do you believe that differential (i.e., so-called "Ramsey") pricing is appropriate in "market-dominant" situations where rates are not in fact controlled by competitive forces? If so, what or who is to control them?

Answer. The issue you raise is very complex one, and the Commission is still searching for an appropriate solution that properly balances the concerns of all parties. In a recent interim decision in Ex Parte No. 347 (Sub-No. 1) Coal Rate Guidelines—Nationwide, we have asked for public comment on this and other issues. The interim decision, a copy of which is enclosed, discusses Ramsey pricing in some detail and the following comments reflect those interim views.

In general, the Commission is committed to the concept of differential pricing. We have always recognized that all commodities cannot and should not be required to make the same contribution to railroad fixed costs, although we have not generally adopted a precise formula or guidelines for achieving this objective. However, we are not satisfied that the railroad-proposed Ramsey pricing is the best form of differential pricing, because this concept would allow perfect economic price discrimination. Each shipper potentially could be charged a different rate based on the shipper's price elasticity subject to the constraint that systemwide earnings could

not exceed a specified level or rate of return. This form of regulation emulates traditional public utility regulation. Unlike the ICC, however, public utility regulators generally have control over the establishment of the entire rate structure. The Commission on the other hand, has no jurisdiction over rates in competitive markets.

This fairly unfettered discretion that the railroads' proposal of Ramsey pricing on a systemwide basis would provide is our principal concern with Ramsey pricing. It would appear that captive shippers could be required to contribute to rail facilities that do not serve them.

However, as indicated above, we have not reached a final decision on this matter, and we will continue to study the question of Ramsey pricing, including variants thereof, such as pricing which focuses on line segments rather than systemwide earnings, as we search for an appropriate methodology to determine maximum reasonableness.

In response to the second part of your inquiry, the ICC has jurisdiction to determine rate reasonableness in situations not controlled by competitive forces, that is market dominanace situations.

Question 6. In determining abandonment applications, what consideration is presently being given by the ICC to the needs of shippers under the "public convenience and necessity" standard?

Answer. In deciding abandonment applications, the Commission weighs the present and future needs for the rail line—and the harm to affected shippers and communities which would result from abandonment—against the present and future burden which continued operation would impose on the railroad and on interstate commerce. In evaluating the burden on the carrier, the Commission considers the profitability or unprofitability of the line, costs of maintaining and rehabilitating the line, current traffic levels and potential for increased traffic, and the opportunity costs the railroad incurs if forced to continue tying up its assets in rail service.

Once the railroad has established that continued operation of the line would be burdensome, the burden of going forward with evidence shifts to shippers to demonstrate their need for rail service and the harm they would incur from its loss. In evaluating shipper interests, the Commission considers the availability and historical use of alternative transportation services, the increased costs of alternative services, future traffic prospects, investment in rail-oriented assets, and claims that the railroad has deliberately discouraged traffic or not provided adequate service.

It should be noted that the Commission's consideration of shipper need is not limited to the individual shippers located on the affected line but also extends to the shipping public in general. When a railroad is forced to continue operating an unprofitable line it may, to stay in business, attempt to subsidize its losses by charging higher rates on more profitable lines. This can impose a burden on interstate commerce, contrary to the public interest. Therefore, the fact that some individual shippers may suffer harm from an abandonment must be considered in conjunction with other factors.

It should also be noted that, where a shipper has a strong interest in retaining rail service, it now has the opportunity to do so under the provisions of the Staggers Rail Act. Under 49 U.S.C. 10905, shippers or other parties may elect to retain rail service after abandonment by either subsidizing the rail operations or acquiring the rail line. They may also acquire rail lines prior to abandonment under the feeder railroad provisions of 49 U.S.C. 10910.

All these factors are closely examined and weighed as they arise in individual cases. The Commission's decision is based on the evidence presented and the merits of the arguments made by the parties.

Question 7. If that standard is being applied fairly and impartially, how could 330 applications for abandonment be approved without a single denial in a 25-month period?

Answer. I believe this is primarily due to the nature of the cases themselves. Approximately forty percent of the abandonment applications decided in the past 25 months were unopposed and, therefore, the abandonments were routinely granted because of no harm to shippers, or statutory mandate (in applications filed after enactment of the Staggers Act). Furthermore, the recent opposed cases have been relatively clear-cut cases that have generally involved lines which are clearly unprofitable or only marginally profitable with heavy maintenance and rehabilitation costs. Many of those cases were opposed by shippers who did not demonstrate an interest in retaining rail service and failed to present a strong case against abandonment. For example, shippers frequently make general allegations that loss of rail service would substantially harm their business operations, without attempting to quantify or substantiate such claims.

In conclusion, the Commission's analysis in abandonment proceedings is based on the evidence and arguments submitted by the parties. If the railroad does not meet its burden of proving that continued operations create a burden to it and interstate commerce, the Commission will deny its application. Once an applicant has shown that continued operations are burdensome, the burden shifts to protestants. Protestants have the opportunity to submit evidence and arguments showing their need for continued service and to contest the railroad's evidence.

I believe that an examination of the records developed in the abandonment proceedings filed over the past 25 months would show that the Commission has fairly and impartially considered and weighed the evidence in each case.

Question 8. If the Commission permits the abandonment of profitable lines on the theory that the investment in the line can be more profitably employed outside the railroad industry, is that not contrary to the national transportation policy?

Answer. At present, the Commission does not permit the abandonment of profitable lines merely because a carrier could earn a greater return on its investment outside the railroad industry. However, the Commission does consider a carrier's opportunity cost as one of the factors to be examined in determining whether the public convenience and necessity permits abandonment. A rail carrier incurs an opportunity cost when it continues to devote its capital assets to rail usage despite the fact that it could earn a greater return on its assets if they were used in an alternative manner.

Almost two years ago the United States Court of Appeals for the Eighth Circuit remanded to the Commission an abandonment proceeding because we failed to consider the carrier's opportunity cost argument. While that case was pending, we instituted a proceeding to determine the appropriate use of opportunity costs as a factor in approving rail abandonments. After analyzing the numerous comments filed, the Commission decided that carriers must be allowed to introduce evidence of their opportunity costs.

I believe the decision to consider opportunity costs is consistent with both the national and rail transportation policies as set forth in 49 U.S.C. subtitle IV. By considering a carrier's opportunity cost, the Commission recognizes the need for financially sound rail carriers. I should also note that to encourage alternate transportation, Congress enacted a provision in the Motor Carrier Act of 1980 which facilitates the entry of motor carriers into markets following rail abandonments, 49 U.S.C. 10922(b)(4)(B).

Moreover, as rail carriers abandon their more burdensome lines there is less need to increase rates on other lines because profitable operations will not have to cross-subsidize less profitable ones.

Question 9. Would you advocate repeal of the provision of section 229 of the Staggers Act which required shippers to file complaints against unreasonable rates by March 30, 1981, or be forever barred?

Answer. I would not advocate repeal of section 229. Indeed, section 229 (which limits shippers' right to challenge existing rates after March 30, 1981) is an integral part of the statutory scheme reflected in the Staggers Act. In particular, section 203, which establishes a zone of rate flexibility, would be unworkable if existing rates could be attacked at any time. To assist the railroads in achieving increased earnings, and to encourage innovative rates, the Staggers Act provides for greater rate freedom. The threat of expensive and time-consuming challenges could discourage the carriers from changing their rates in response to market conditions or to cover inflationary costs. On the other hand, freedom to increase rates assumes a reasonable rate structure. It is for that reason the savings provision was included in the Act.

Question 10. As a matter of fact, are there not reasonable grounds for believing that denying a shipper the right to complain about an unreasonable rate at any time is an unconstitutional taking of property without due process of law?

Answer. Denying a shipper the right to complain about an unreasonable rate at any time is not an unconstitutional "taking" of property without due process of law. A "taking" is a government action which appropriates some recognized properety right of an individual or business for public use. See *Penn Central Transp. Co.* v. *New York City,* 438 U.S. 104, 123–125 (1978). Here, however, no appropriative action is taken and no property right is involved.

The effect of section 229 is merely to permit certain ratemaking activity without government interference. The Fifth Amendment protects against direct appropriations only Where the government is merely imposing (or, as here, removing) regulations of general applicability which happen to affect a particular party economically, there is no "taking" under the Fifth Amendment. *Condor Operating Co.* v. *Sawhill,* 514 F.2d 351, 361 (Em. App. 1975), cert. denied, 421 U.S. 976 (1975) (and cases cited there).

Furthermore, there is no constitutional right to protection from "unreasonable" railroad rates. Government review of rate reasonableness (and protection from unreasonably high rates) was instituted by statute. Congress has the authority to limit or eliminate this legislated program (as it did inter alia in section 229). In our view, shippers do not have a sufficient property interest in being able to challenge the reasonableness of existing rates to support a "taking" claim here.

Question 11. As I understand it the railroads generally take the position that the Commission should not interfere with their managerial pricing judgment on particular traffic, however profitable, until they become revenue adequate on an overall system basis. Do you believe that there should be an "open season" on captive traffic no matter how efficiently or inefficiently any particular railroad may be operated or no matter how successful its efforts to minimize losses and maximize profits on noncompensatory traffic?

Answer. The Commission certainly has never taken the position that there should be an "open season" on captive traffic. As indicated in our answer to prior questions, the Commission attempts to administer faithfully the laws entrusted to it, in accordance with the intent of Congress.

Revenue adequacy is an extremely important consideration. However, revenue adequacy standards under § 10704 also require consideration of "honest, economical and efficient management," and other provisions of the Staggers Act require the Commission to consider the amount of traffic transported at revenues which do not contribute to going concern value and the extent to which rates which contribute only marginally to fixed costs can be changed to maximize the revenues from such traffic. Thus, we do not believe there is a basis for the reference in your question to an "open season" on captive traffic.

Question 12. The Commission recently has taken a number of steps to stimulate long-term transportation contracts, now clearly authorized by the Staggers Act. At the same time the Commission has taken a number of actions which probably will further restrict its jurisdiction, for example, product and geographic competition as market dominance tests. Will you not agree that these two concepts are counter-productive? In other words, how can a captive shipper bring a railroad to the bargaining table unless the shipper still retains the option of rate litigation before the Commission?

Answer. We do not believe that encouragement of contracts, as intended by the Staggers Act, and consideration of product and georgraphic competition as tests of market dominance are counter-productive. To the extent that a shipper is captive, that shipper still has recourse to the Commission if it believes its rates are unreasonably high. Thus, to avoid litigation on this issue and the possibility that the Commission would order a reduced rate, the rail carrier does have an incentive to negotiate a contact acceptable to both parties.

Our market dominance regulations are intended to identify captive shippers. If in fact product and geographic competition exist for a given shipper, that shipper would not be captive because it would have alternatives available. If that is the case, the rail carrier likewise would have an incentive to negotiate a contract out of concern that it might otherwise lose the traffic. Thus, in either situation, the rail carrier has the incentives to attempt to reach acceptable contract rate provisions with the shipper.

Question 13. The Long-Cannon amendment embodied in Section 203 of the Staggers Act calls upon the Commission in determining rate reasonableness both for investigation and complaint proceedings to consider whether the carrier is transporting noncompensatory traffic, has maximized the contribution of marginal traffic and the carrier's mix of traffic to insure that no commodity makes an unreasonable contribution to the railroads' total revenues. I'm told that the data that will make possible this consideration is within the possession of the railroads. Should not the Commission take some action to require that this data be made available so that the provisions to which I refer can be implemented?

Answer. On December 11, 1981, a number of utility companies filed a petition for a rulemaking proceeding to implement the Long-Cannon amendment [49 U.S.C. 10707a (e)(2) (B) and (C)]. The petition is docketed as No. 38754. Petitioners contend that the Commission lacks data necessary to comply with these provisions.

As this is a pending proceeding, it would be inappropriate to comment on the matter in any depth. It is clear however, that the issue of possession of the necessary data will be addressed in any ruling on the petition.

Senator DANFORTH. Thank you very much, Mr. Taylor.

The next witness is William H. Dempsey, president of the Association of American Railroads.

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STATEMENT OF WILLIAM H. DEMPSEY, PRESIDENT, ASSOCIATION OF AMERICAN RAILROADS

Mr. Dempsey. Thank you very much, Mr. Chairman.

I appreciate the opportunity to review with you briefly our appraisal of the workings of the Staggers Act.

I think as you look at our complete statement, you'll see that in our view the act is working pretty well. I want to second Mr. Blanchette's endorsement of the way that the Commission has, by and large, proceeded. They have acted expeditiously and, we think, by and large within the objectives of the act.

There are some clouds on the horizon. I would agree with Chairman Taylor, however, that it would be premature for Congress to take any action because, for the most part, these matters are still before the Commission or are in litigation. In the limited time available today, I would like to focus on a couple of those clouds.

The act of course was a legislative landmark. It was the most important act for the railroads since the original Interstate Commerce Act. It evidenced, I think, the view of Congress that regulation has become the problem and not the solution for the rail industry. We lost the monopoly position that brought about the enactment of the Interstate Commerce Act in the first place, and we were on the road, it appeared, to nationalization. It looked as if Penn Central would be replicated by the Rock Island and the Milwaukee, and throughout the country.

I won't take the time to review the major provisions of the act because you're well aware of them. But basically the purpose was, insofar as possible, with adequate protection of shippers, to put the railroads in a position to manage their assets like other businesses in the United States.

It was a long drawn-out struggle. There were contests and opposition by a number of elements in the shipping community. But in the end, I think almost everybody involved agreed that the compromises that had been reached were suitable.

Now, I expect here, during the course of this hearing, that because the rails are now doing quite well, there will be talk about record earnings. Conrail, for example, had a so-called record third quarter. That is to say, it didn't lose anything in the third quarter; it made a modest profit, but one that is hundreds of millions of dollars below an adequate revenue level.

The Chessie was another railroad that had a good third quarter—in 1980 the Chessie earned less than 7 percent on its investment, a little more than half of the return that the Commission has established as an adequate revenue level. The point I would like to make is this. If we don't hear in the next several years, repeatedly, talk about record railroad revenues, then the Staggers Act would have been a failure.

The adequate revenue determination by the Commission is a critical determination. It determined, under the relevant provisions of the act, that in 1980 the rails would have to earn 12.1 percent to earn adequate revenue levels. Now, that proceeding is ongoing and, with the rates of return on the money markets as they are, we think it ought to be upward of 18 percent. At any rate, it has to be upward, certainly, of 12.1 percent.

Keeping that figure in mind, look at what the Commission found in its 1980 determination on revenue adequacy. It looked at 37 railroads, and it found 20 of those earning less than 7 percent, 12 earning less than 4 percent, only 8 earning more than 9 percent, and only one of those 8 was a major railroad. And only three railroads in the whole United States were found to be earning more than the adequate revenue level of 12.1 percent; and all of those three were small railroads. So, we've got a long way to go.

We did have, in the 12 months ending in June, an overall rate of return of about 4½ percent—4.56 percent to be exact. That's a record for us. But that's not a record for anybody else in the United States. So, that's still far below what the rails ought to be earning.

But still, I must say there's been some progress. At the same time, you're looking at this enormous inflation element. And so, while we made some progress up the ladder, the ladder has gotten longer. So, I can't really say whether we're better off in this 12-month period or marginally worse off.

Now, for our main concerns—we have a couple:

One, you have already focused on, so I won't belabor the point. I was gratified to hear the chairman's response to your questions about the guidelines for determining what a maximum reasonable rate is. The fact of the matter is that if we cannot on any rate earn more than fully allocated costs, as the Commission has defined it, we would have lost our ability to price differentially.

We have received from the Commission a pretty good definition of "adequate revenue levels." That is to say, the "current cost of capital." That's the standard on which every business in the United States is measured. Having developed a good definition of "adequate revenue levels," it makes no sense for the Commission to define "maximum reasonable rate" so as to make it impossible for the rail industry ever to achieve adequate revenue levels.

I won't go into the details as to why it would be impossible for the railroad's ever to earn adequate revenues if rates were limited to fully allocated costs, but I do in my statement. You're familiar with the statement. I think every responsible economist in the country would agree with the conclusion that I've just stated. So, as I say, all that we can do is to hope that the Commission will proceed in a manner that recognizes that reality

The second problem that we have is the deluge of cases that have been brought under the savings provision of the Staggers Act. We have a cost recovery index, as you know, under the Staggers Act. That has been very helpful to us. Over the course of the 2 years prior to the Staggers Act we have lost something in the way of $3 billion in revenue because of our inability to recapture our cost increases in a timely fashion. The correction of that problem was perhaps, in the short run, the most important achievement of the Staggers Act.

Under the cost recovery index procedure a railroad can raise any rate by the amount of the index without challenge by a shipper. Obviously the right to raise a rate by that amount would have been illusory if the shipper had retained the right to challenge the reasonableness of the underlying rate. So, the Congress—quite

properly, we think—provided an opportunity to shippers within a 180-day period to challenge existing rates.

But I don't think that anyone contemplated that there would be some 800 or more complaints filed involving thousands of rates on whole segments of traffic. But that in fact has happened. Rates that have gone unchallenged for years have been brought into question in these hundreds and hundreds of complaints.

This is an administrative nightmare and it is potentially a dire threat to the railroads. The success of any significant number of these complaints would seriously impair rail earnings and, if the Commission were to apply in these proceedings its proposed fully allocated cost ceiling, the result would really be calamitous to the industry.

Again, we think that the impact is so obvious that we can only hope that the Commission will recognize it and that the threat that we see will not be realized.

I think that's all I have to say, Mr. Chairman. I appreciate the opportunity to be here.

Senator DANFORTH. Thank you very much, Mr. Dempsey.

I have one question that's been handed me by Senator Long's staff, from Senator Long. It reads as follows:

> I am told that the railroads now espouse an economic theory that is referred to as "Ramsey pricing." Am I correct that this theory amounts to saying that the greater the degree of railroad monopoly power over a particular traffic, the higher the rate that should be permitted?

Mr. DEMPSEY. I think I'd better say no.

Senator DANFORTH. I'm sure that Senator Long will be relieved to know that.

Mr. DEMPSEY. I suppose, Mr. Chairman—I don't really know what "Ramsey pricing" is—but I suppose that perhaps it's another way of referring to differential pricing. And as for that, I would say that we firmly endorse the notion of differential pricing.

Indeed, it's the other side of the fully allocated cost question. And in our judgment—and I think, as I say, in the judgment of all economists—differential pricing is really in the best interest of all of our shippers. What happens is this. If we can recover more than our variable costs on competitive traffic, that means that that traffic is contributing to the fixed costs of our enormous plant. And that means that the so-called captive shippers have less to bear of those fixed costs.

If we're forced to abandon differential pricing, we lose that contribution from the competitive elements of our traffic, and everyone is going to suffer, and we are going to be faced with these hearings time and time again.

[The statement follows:]

STATEMENT OF WILLIAM H. DEMPSEY, PRESIDENT, ASSOCIATION OF AMERICAN RAILROADS

Mr. Chairman and members of the subcommittee, I appreciate this opportunity to review with you the railroads' first year of experience under the Staggers Rail Act of 1980. While all of the evidence is not yet in, the Act appears to be fulfilling many of the Congress' expectations and the railroads are hopeful that the purposes of the Act will, in time, be achieved. To provide the necessary perspective for my comments on our experience to date under the principal substantive provisions of the Act, I would like to recall for you the impetus for, and purposes of the Act.

The impetus for the Act was the mounting evidence that the economic decline of the railroad industry—evidenced by chronically low earnings, shortfalls in capital investment, and numerous bankruptcies—was not going to be halted as long as the railroads continued to be stifled by a blanket of government regulation. The tentative beginning under the 4-R Act of 1976 was plainly insufficient.

Thus, it became the purpose of the Staggers Act "to provide for the restoration, maintenance, and improvement of the physical facilities and financial stability of the rail system of the United States." (section 3) In pursuit of this purpose, a new rail transportation policy was enunciated. The first six paragraphs of the policy section provide a trenchant statement of what the Staggers Act is all about. In summary, it is the policy of the Congress to rely principally on competition and demand for services in establishing reasonable rates, to minimize the need for regulatory control, to ensure development of a sound rail transportation system, to allow carriers to earn adequate revenues, to assure effective competition among and between the transportation modes, and to maintain reasonable rates where there is an absence of effective competition or where revenues exceed the amount necessary to maintain the rail system and attract capital. (section 101(a)) Consistent with the Act's finding that "today, most transportation within the United States is competitive," regulatory controls were to be replaced by market forces to the fullest extent possible and, where regulation was required, the need for achieving an adequate revenue level was to be a major consideration. The principal substantive provisions of the Act deal in one way or another with these two concerns—substituting the forces of competition for regulation and permitting the achievement of adequate revenues.

ESTABLISHING THE STANDARD FOR ADEQUATE REVENUES

Because a principal purpose of the Act was to permit the achievement of adequate revenues by rail carriers, one of the first proceedings instituted by the Commission following enactment of the Act was Ex Parte 393, Standards for Railroad Revenue Adequacy. In that proceeding, the Commission determined that the appropriate standard was a return on investment equal to the railroads' current cost of capital. The enuniation of such a standard was not surprising since it is precisely the standard by which the success of every other business in the United States is measured. The Commission's decision in Ex Parte 393 is on appeal in the 3rd Circuit on various grounds. We believe that, on the central issue, the Commission's decision is clearly correct and entirely consistent with the Act, and expect that the court will so find.

In its latest determination, the Commission found that the railroads' cost of capital was 12.1 percent in 1980 and that only three small railroads were earning adequate revenues. While there has been some improvement in railroad earnings—the rate of return on investment for the industry increased from 3.07 percent for the year ending June 30, 1980 to 4.56 percent for the year ending June 30, 1981—the industry still has a long way to go and, while one might hope for a permanent reversal in the trend, the cost of capital has continued to soar for railroads as it has for American industry generally. We estimate our current cost of capital to be about 18.6 percent. The Commission's next determination of an adequate revenue level should, therefore, be substantially higher than the 1980 determination of 12.1 percent. Because of the continuing increase in the cost of capital, one cannot be certain that the industry is substantially further along than it was one year ago in achieving adequate revenues. Although we are making some progress in climbing the adequate revenue ladder, the ladder has been getting longer.

I would like to stress the point that the railroads are not expecting any guarantees with respect to revenue adequacy. In times of economic slack, healthy rates of return on an industry-wide basis may not be possible to achieve under any circumstances. But the flip side of that coin is that in good years better than adequate rates of return should be expected. The one thing the railroads cannot tolerate is a regulatory policy which precludes any good years. That is the same treadmill the railroads were on from 1920 to 1980 and the basic purpose of the Staggers Act was to get us off of that treadmill.

This leads me to the most serious criticism we have to offer with respect to the Commission's administration of the Staggers Act. The Commission has proposed to adopt—and has actually applied in several cases—a maximum rate reasonableness standard that is so clearly erroneous, and so clearly self-defeating in terms of meeting the revenue adequacy goal, as to be absolutely baffling. Let me explain our consternation.

In its decision in Ex Parte 393 establishing the current cost of capital as the standard of revenue adequacy, among the comments made by the Commission were the following:

"Funds flow analysis and other minimum standards of revenue adequacy . . . are inappropriate as indicators of long term revenue adequacy and are especially inappropriate as measures to limit rail pricing flexibility which is one of the roles the Rail Act accords revenue adequacy findings . . . In short, we would be assigning the railroads the Sisphyean task of working toward revenue adequacy, and every time it came close robbing it of the very means it had used to get there.

"The standard we will use to measure the adequacy of the rate of return is the current cost of capital. Such a standard is widely agreed to be the minimum necessary to attract and maintain capital in the railroad, or any other, industry. . . . If a firm is unable to earn the cost of capital, investors will be unwilling to supply capital to it.

"Once again, we want to make it clear that we will not and cannot guarantee any railroad a return equal to the cost of capital. A railroad, like any other firm, should earn such a return only if it provides a desired service in an efficient manner. *We want to take great care, however, not to deny railroads the opportunity to earn the cost of capital.*" [italic supplied]

Having said all of this in its Ex Parte 393 decision, the Commission has proposed in Ex Parte 347 (Sub-No. 1), Coal Rate Guidelines Nationwide, to establish a maximum rate reasonableness standard that would deny the railroads the opportunity to earn adequate revenues. Indeed, under the Commission's approach the railroads would be required to reduce their revenues and it is doubtful whether some railroads could even survive. The standard being proposed would limit a rate to the fully allocated cost of the movement calculated on a ton/ton-mile basis.[1] The adoption of a fully-allocated cost standard is nothing other than a rejection of differential pricing, which is pricing based on the demand for services. And without differential pricing, the railroads cannot expect ever to achieve an adequate revenue level.

The Congress recognized this fact when it enacted the Staggers Act. As I noted at the outset, it was stated as a basic policy of the Act that the Government should "allow, to the maximum extent possible, competition and the demand for services to establish reasonable rates." Various sections of the Act are explicitly or implicitly designed to permit market pricing to work.

The House Committee in its report on the Act stated the rationale for differential pricing:

"Because of the existence of competition, all rates cannot pay an equal percentage of 'fixed costs.' As in other industries, some rates will contribute more to fixed costs than others. The Committee understands the necessity of such differential pricing, and has designed a regulatory system which allows for such pricing decisions. In the absence of the regulatory flexibility which permits differential pricing, all shippers would be harmed. If traffic which moved at low rates were forced to pay higher rates, the traffic would disappear to other modes. When the traffic moved to another mode, the contribution to fixed cost made by that traffic would also disappear. The result is that the remaining commodities would have to make up for the fixed cost formerly paid by the traffic which moved to another mode, resulting in higher rates for the remaining traffic." (pp. 39–40)

Differential pricing is the only means of assuring that railroads earn sufficient revenues to provide adequate service; therefore, it is the pricing system that is most fair to all shippers. The "captive" shipper benefits in the long run from the revenue contribution made by the "non-captive" shipper; and the non-captive shipper retains access to a rail service that would otherwise not be available to him. The principle of differential pricing has also been accepted by the Commission virtually since its inception. In a coal case decided in 1977, it stated:

"We recognize that since much railroad traffic moves at rates below fully allocated costs because of competitive pressures, a railroad must be allowed to set some rates in excess of their full cost level where competition, market conditions, and demands permit." (357 I.C.C. at 700)

So I repeat, we find the Commission's proposed policy to be absolutely baffling, particularly because of the disastrous consequences of pursuing such a policy. In their comments in Ex Parte 347 (Sub-No. 1), the railroads have provided the follow-

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[1] While the Commission has characterized this as a fully allocated cost standard, that is a misnomer because, in fact, the Commission is prohibiting the full allocation of costs. Under the Commission's approach, a large body of costs would never be allocated to any movement and, thus, never recovered by the railroad.

ing estimates of the effect of the Commission's proposed policy where it applied to all heavy-loading commodities and not just coal.

For the roads in the West, applying this policy to their 1979 traffic would have resulted in a decrease in revenue of more than $1.6 billion. The effect of a loss such as that can be shown by comparing it with the pre-tax net income of the Western roads in 1979 which was only $678 million. In 1979, the return on investment for the Western roads was only 4.38 percent.

For five of the major roads east of the Mississippi River the loss of 1979 revenues would have been:

	Million
Conrail	$387
Chessie	231
Family Lines	229
N. & W	170
Southern	157
Total	1,368

The effect on the 1979 rates of return of these roads would have been:

[In percent]

	Actual 1979 ROR	With proposed policy
Conrail	−24.68	−44.14
Chessie	3.70	−3.16
Family Lines	5.27	−2.30
N. & W	7.97	3.23
Southern	6.99	3.47

One need not elaborate on the effects on Conrail in 1979 or any other year of a $387 million reduction in revenue. In testimony before the Commission, L. Stanley Crane, the Chairman of the Board of Conrail, put it succinctly: "The Commission's proposed rate guidlines will destroy any chance Conrail has of attaining revenue adequacy. Not only would massive federal funding be required in the immediate future, but it would continue to be necessary indefinitely." It is clear that, with the Commission's standard, no one would want to buy Conrail.

In addition to the coal rate guidlines proceeding now pending before the Commission, the issue is before the courts as a result of the application of the proposed policy in individual rate cases. Fortunately, the railroads are not standing alone in their questioning of that policy. In an appeal brought in the D. C. Circuit by the Burlington Northern and Missouri Pacific, in which the United States as well as the Commission are named as respondents, the Department of Justice has filed a brief on behalf of the United States which in effect agrees with the appellant. One passage from that brief summarizes the problem very well:

"The decision of the Commission in this case contains legally inadequate findings to support its conclusion that the maximum reasonable rate for the Redfield coal movement at issue should be at a level equal to the fully allocated costs of the movement as computed pursuant to the ton/ton-mile allocation method (or the Commission's jurisdictional threshold, whichever is higher). First, the Commission wholly failed to explain in its decision how use of the ton/ton-mile allocation method, which is essentially an accounting convention for computing the 'full costs' of a particular movement based on the weight of the freight and the length of the haul, can rationally measure the maximum reasonableness of any particular rate, including the Redfield rate. Second, although the Commission has repeatedly stressed that railroad revenue adequacy is a 'highly important' factor to be considered in railroad rate proceedings, the Commission failed to specifically consider and address this relevant concern in this case. Indeed, the Commission wholly ignored the evidence and contentions submitted by the parties in this case as it relates to the railroads' specific revenue needs and the railroads' ability to generate sufficient revenues from traffic other than the Redfield movement."

With the Government helping us argue the merits of our case, we are hopeful that the outcome will be one fully consistent with the intent of the Act.

MARKET DOMINANCE

In another proceeding instituted shortly after enactment of the Staggers Act, Ex Parte 320 (Sub-No. 2), the Commission proposed to revise its regulations with respect to determining market dominance. In implementing the market dominance provision of the 4-R Act of 1976, the Commission had established three rebuttable presumptions of market dominance—whether the rate was more than 160 percent of variable cost, whether the carrier handled 70 percent or more of the traffic, and whether the shipper had made a substantial investment in rail-related equipment which prevents the use of another carrier or mode.

With enactment of the Staggers Act, a new statutory threshold based on the revenue-variable cost percentage was established. However, the original market dominance provision of the 4-R Act was left intact and thereby became an additional threshold. Consequently, even if the rate exceeded the revenue-variable cost threshold, the Commission might still be able to find that there was effective compitition for the traffic. Thus, the Act clearly compelled the reexamination which the Commission undertook in Ex Parte 320 (Sub-No. 2).

After receiving extensive comments from interested parties, the Commission issued this past July new guidlines for determining market dominance. In those guidelines, the Commission did not rule out consideration of factors such as market share or substantial investment made before October 1, 1980. It did, however, eliminate any presumption with respect to those factors. With respect to substantial investments on rail equipment occurring after October 1, 1980, the date on enactment of the Staggers Act, the Commission concluded that a shipper making such an investment should avail itself of the contract provisions of the Act rather than seek continued regulatory shelter from the Commission.

In its guidelines, the Commission has addressed the four major forms of competition that affect rail transportation, i.e., intramodal, intermodal, product, and geographic. Product competition arises from the ability of shippers or receivers to utilize a substitute product; geographic competition arises from their ability to obtain the same product from a different source or to send it to a different destination. Detailed guidance has been provided for assessing the presence or absence of these four forms of competition. Evidence as to other forms of competition is not, however, ruled out.

So, in effect, the Commission has rejected presumptions, which it had found to be not sufficiently reliable, and substituted a case-specific examination of all relevant evidence bearing on the question of whether competition exists with respect to a particular movement. The railroads support the Commission in this approach. We believe it represents a legally sound and administratively feasible implementation of the Act.

Those shippers who object to this approach argue that it does not provide a "practical determination without administrative delay" as contemplated by the 4-R Act. The fact is that the "quick" determination urged by the 4-R Act has been provided in the Staggers Act through the newly-created revenue-variable cost percentage threshold test. With a quick test having been statutorily created, we believe the Commission has correctly perceived that any further analysis of the "absence of effective competition" for traffic above the statutory revenue-variable cost threshold can only be accomplished by examining whatever may be the competitive factors bearing on the movement. Presumptions are unnecessary in this situation. When, as here, they have been found to be unreliable, they are pernicious as well.

Some shippers have also argued that the consideration of product and geographic competition is not permitted by the Act. We believe the Commission is clearly correct in rejecting that argument. Product and geographic competition have long been recognized by the courts, commentators, and the Commission itself as significant forces which constrain rates. There is nothing in the law, the legislative history, or logic to suggest that Congress intended to limit the Commission's discretion in determining what constitutes "effective competition."

As you may know, the Commission's decision in Ex Parte 320 (Sub-No. 2) has been appealed so a final verdict is yet to be rendered on this subject.

ZONE OF RATE FLEXIBILITY

Section 203 of the Staggers Act establishes a zone of rate flexibility to permit rail carriers the opportunity to recover their inflation-based cost increases without challenge and with minimal delay or regulatory interference. This inflation-based cost recovery increase was provided simply to keep the railroads earnings from deteriorating due to inflation. To give carriers an opportunity to increase their earnings and move toward revenue adequacy, the Act also permits them to raise

their rates 6 percent above the inflation-based increase.[2] A shipper can obtain Commission review of these above-cost increases but, unless the rate is being raised above 185 percent of variable cost,[3] the burden of proof as to the reasonableness of the increase is on the shipper.

The cost recovery increases under Section 203 are pegged to the rate of cost inflation experienced by the railroad industry. Congress directed the Commission to measure this inflation using an "Index of Rail Costs." The selection of an appropriate index was left to the Commission's discretion except that the index was to be adjusted "to reflect the changing composition of railroad costs, including the quality and mix of material and labor."

The Commission found the most acceptable measure of changes in rail costs to be the input price index compiled by the AAR. (Ex Parte 290 (Sub-No. 2)). Additionally, to comply with Congress' mandate that the index reflect the changing composition of railroad costs, the Commission required that the weights applied to the various inputs used in calculating the index be updated annually. This reweighting of the index's cost components accounts for all changes in the importance of each input as a percent of total railroads costs.

A fundamental purpse of the index was to remove the regulatory burden and delay inherent in prior cost recovery procedures, and thereby allow the industry to cover the effects of inflation more fully and more promptly. Prior to the Staggers Act, regulatory lag in implementing general rate increases had inflicted enormous revenue losses on the railroad industry—amounting to more than $3.3 billion between June, 1978, and July 1980.

In enacting 203, Congress considered how to eliminate this regulatory lag and how extensively the index should be adjusted each quarter in light of the need to provide an efficient cost recovery procedure. Some parties urged Congress to require adjustments to reflect virtually every conceivable aspect of changes in railroad total and unit costs, while others preferred that the index not be adjusted at all. Congress, however, chose a middle ground, requiring adjustments to reflect those aspects which produce changes in the composition of railroad costs. The Commission has properly implemented these adjustments, and the index it has approved therefore does reflect these changes.

Certain shippers have appealed from the Commission's decision on the index to the Court of Appeals for the D.C. Circuit. The Commission, the Department of Justice, and the AAR have all defended the decision, and we believe that it will be upheld by the Court.

As might be expected, a few technical issues not previously considered by the Commission have arisen since the Commission's decision establishing the index. The Commission has therefore reopened the Ex Parte No. 290 (Sub-No. 2) proceeding to consider how interest on wage increases that have been recovered but not disbursed should be handled, and possibly other related matters. The AAR expects that these issues will be resolved in a manner which is satisfactory to all interested parties.

Contrary to the fears expressed by many shippers at the time the Staggers Act was being considered by the Congress, the zone of rate flexibility created by section 203 has not led to rampant rate increases by the railroads. Inquiries we have made of several railroads indicate that relatively few increases have been taken under the 6 percent provision in the past year. Most increases have apparently been limited to cost recovery and taken in the form of general rate increases.

With respect to individual rate actions, data supplied to us by the three railroad rate bureaus indicate that the pricing flexibility provided by the Staggers Act has led much more often to rate decreases than to rate increases. In the West during the period April through September, 1981, there were 544 rate increases and 10,027 rate decreases. In the East, there were 510 increases and 3,037 decreases. In the South, there were 376 increases and 359 decreases. The railroads' willingness to reduce rates to meet specific traffic opportunities is attributable directly to their ability under the Staggers Act to raise rates when conditions change or expected traffic does not develop.

The effect of the restrictions placed on collective ratemaking by the Staggers Act also are apparent in the data provided by the rate bureaus.[4]

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[2] After four years the level is reduced to 4 percent and limited to carriers with inadequate revenues.

[3] Rising to a maximum of 190 percent on October 1, 1982.

[4] Revised rate bureau agreements are still pending approval by the Commission and, at this time, application of the "direct connector" ratemaking restriction contained in section 10706(a)(3)(A)(iii) has been completed only in part under the Commission-ordered phase-in. Under these circumstances, it is too early to make any final assessments with respect to the changes in collective ratemaking being effected pursuant to the Staggers Act. If serious prob-

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In the South during the period October 1, 1979, to October 1, 1980, there were 1770 individual carrier rate change announcements. In the period October 1, 1980, to October 1, 1981, there were 3,569 individual rate change announcements. Prior year figures were not available in the East and West but the preponderance of independent action is evident from the data for the period April through September, 1981. In the East during that period there were 3,299 independent announcements and only 248 rate bureau actions. In the West during that period there were 9,091 independent actions compared to 1,503 rate bureau actions.

Many examples could be cited of how the pricing freedoms provided by the Staggers Act are working to the advantage both of the shippers and the railroads. This year, for example, there has been a considerable surplus of grain-carrying cars as farmers have stored much of their grain in hopes of obtaining better market prices later. Railroads have responded to this by cutting many of their grain rates in order to stimulate business.

Last spring, the Soo Line offered to give grain shippers two free moves for every ten carloads received. So successful was the program that the Soo had to take out of storage 1,000 grain cars that had been idled.

Conrail is putting particular emphasis on some shorter haul moves that frequently move by truck. The cost of one particular 200-mile move, for example, was reduced from $1,368 to $585.

Conrail has also moved aggressively under deregulation to reduce the number of empty backhauls it has historically had. Seeing that it was returning many empty cars to Canadian National, it reduced backhaul rates on CN boxcars as much as 35 percent.

Other backhaul reductions have covered movements to connecting U.S. roads in the South and Southwest. Furniture rates to the Southwest, for example, were reduced 20 percent. In one hypothetical move, that meant savings of more than $600 for moves from Boston to Dallas.

The backhaul rate program has succeeded both in gaining new business for Conrail and in reducing the number of empty backhauls. During the first two years of its existence, it was credited with bringing $7 million worth of new business to Conrail. Connecting lines also gained new revenues.

Chessie recently announced rate reductions for boxcar movements to the East in an effort to better balance traffic flow.

Many innovations as well as rate reductions are coming under the freer climate fostered by the Act. Chessie has worked with the water transport subsidiary of Dravo Corporation to develop a new intermodal transport package involving the movement of import products via ocean vessel, river barge, rail car, and truck under a single through-service rate.

The new Act is also encouraging reductions in the paperwork burden on shippers and railroads. Family Lines has scrapped the maze of intermodal tariffs it previously had and replaced them with a simple, four-page price list that allows a shipper to determine quickly what the cost of transport will be.

The Act is also being used to preserve service that might otherwise have been eliminated. Both Southern and Missouri Pacific, for example, have reached agreement with major shippers to preserve and improve lines that had been targeted for abandonment before passage of the Staggers Act.

In short, the ratemaking flexibility provisions of the Act are working and not just to the benefit of the railroads but to the shippers as well.

SAVINGS PROVISION

In granting the carriers the right to take inflationary cost increases without challenge from a shipper, it was necessary to prohibit the shipper from challenging the reasonableness of the underlying rate. Because the existing rate structure had been in place for years, had been open to challenge and, most importantly, was yielding grossly inadequate revenues, the Congress presumed it to be reasonable. The purpose of the savings provision was "to give affected parties a final opportunity to review the reasonableness of existing rates before their opportunity to challenge those rates is curtailed." (Conference Report at 121)

I do not believe anyone anticipated the avalanche of complaints engendered by this "final opportunity." It was taken as an open invitation to what has become known as the "hunting season" and has created an administrative monstrosity for the Commission. More than 800 complaints have been filed under section 229 involving thousands of rates. Complaints were filed on rates that had gone unchal-

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lems develop in the light of this current experience, we would expect the Commission would use the discretion granted to it under the Act to deal with them.

lenged as to their reasonableness for years. Many of the complaints involve large blocks of rail traffic; consequently, rail earnings would be severely impaired were any significant number of the complaints to be sustained by the Commission. Were the Commission to apply its proposed maximum reasonableness standard in these proceedings, it would cost the industry hundreds of millions of dollars—a result that would be absolutely catastrophic. We find it hard to imagine how such a wholesale assault on a rate structure that is currently yielding inadequate revenues can succeed. We can only hope that the Commission is of the same persuasion.

CONTRACTS

In commenting on section 208, the contract provision of the Staggers Act, the Report of the Committee on Conference stresses the point that "the establishment of contract rates is a significant aspect of the new freedom allowed to carriers to market rail transportation more effectively." (at 100). The evidence indicates that the Committee's expectation is being realized.

Under section 208 of the Staggers Act, railroads and shippers are permitted for the first time to enter into enforceable transportation contracts. The railroad industry regards this provision as one of the more beneficial aspects of the legislation, and I believe it is so regarded by the shipping community as well. As long as a contract service does not impair a carrier's ability to meet its common carrier duties, contracts may be utilized to afford shippers service and equipment commitments while affording the railroads a level of compensation which will provide an adequate return on investment. Innovative use of the contract rate mechanism permits a carrier to produce rail transportation service more closely attuned to the specific needs of individual shippers and enhances the competitive opportunities for both the carriers and the shippers.

There are about 600 transportation contracts on file with the Commission. This number is not large in terms of the total amount of rail service being performed, largely because the contract approach is still relatively new both to the railroads and the shipping community. The use of transportation contracts is on the rise, however, and in time should become a major factor in rail transportation.

A review of the contracts on file with the Commission supports our optimism. First of all, the use of contracts is widespread, forty-four railroads have entered into contracts with their shippers. Secondly, the contracts cover transportation of some 129 different commodities so their utilization is not being limited to a few special situations. Finally, the duration of the contracts varies tremendously—ranging from 39 days to 20 years—which is another indication of innovative use tailored to marketing conditions. A few examples demonstrate the variety of contract usage.

The Chessie and Illinois Central Gulf are involved in one contract that utilizes unit trains and eliminates the empty backhaul. ICG moves a unit train of phosphates from the Gulf of Mexico to Chessie, which delivers it to Midwestern fertilizer plants. Chessie then reloads the train with grain and delivers it to ICG, which takes it back to the Gulf for export.

Contracts are also making it possible for railroads to put together other deals that permit them to compete even on some short hauls. For example, Conrail has one contract calling for the movement of 14-car trains of tank cars be between two New Jersey plants less than 20 miles apart. That business went by truck previously.

Southern Pacific has contracts with a number of shippers in which service reliability, rather than speed, is the goal. Service contracts between Portland and the Los Angeles area call for SP to provide four-day service; other contracts cover different SP points. Since this program was begun, business has improved and reliability has gone from about 60 percent to 85 percent.

One of the more innovative coal contracts is a 20-year agreement between Illinois Central Gulf and Hoosier Energy. Hoosier is advancing $9 million to ICG so that its rail line can be improved. In return, Hoosier gets access to the coal it needs and receives more favorable rates than otherwise would have been possible.

One aspect of the Commission's interpretation of section 208 gives the railroads great concern. In section 208(i), Congress provided that the "exclusive remedy" for "any" alleged breach of a contract shall be in a state or federal court. Any pre-Staggers Act contracts, if lawful, are to be treated the same as post-Staggers Act contracts (section 208(j)). Congress clearly intended that issues of contract enforcement be reserved for the courts. The Commission has asserted, however, that as to rate contracts allegedly entered into prior to the Staggers Act, it retains jurisdiction to prescribe a maximum rate equal to the contract rate level even where that level is below the jurisdictional threshold. The railroads believe that the Commission's approach is doubly unlawful—first, because it in effect enforces an alleged contract when such issues are reserved for the courts; and second, because it holds maximum

rates below the jurisdictional threshold. The issue is being litigated and, hopefully, the railroads' interpretation of the Act will be upheld.

The Commission has instituted a proceeding to prescribe rules for rail transportation contracts, but final rules have not yet been promulgated. We can only assume at this time that the final rules will encourage rather than stifle what appears to be a solid beginning in the use of this particular marketing tool.

EXEMPTIONS

Section 213 of the Act broadened substantially the exemption power first granted the Commission in the 4-R Act of 1976. Exemptions from any provision of subtitle IV of title 49, United States Code, are now permitted when the Commission finds that the provision is not necessary to carry out the national transportation policy and the transaction or service is of limited scope or not needed to protect shippers for an abuse of market power. The Conference Report urged the Commission to "pursue partial and complete exemptions from remaining regulations," and went on to state:

"Particularly, the conferees expect that as many as possible of the Commission's restrictions on changes in prices and services by rail carriers will be removed and that the Commission will adopt a policy of reviewing carrier actions after the fact to correct abuses of market power." (at 105)

The first significant exemption since the enactment of Staggers was that granted all piggyback traffic (TOFC/COFC). That exemption appears to be working quite well.[5] For example, BN has reduced single container rates for export traffic to ports in the Pacific Northwest in an effort to gain new business. It is also offering special backhaul rates in an effort to fill empty trailers or containers moving from Texas, Oklahoma, and Colorado to either Chicago or the Northwest.

N&W is another road that has reduced some piggyback rates. In this case, the objective is to increase its export business moving between the Midwest and East Coast ports.

Other roads have offered improved service under deregulation. Chessie has inaugurated a non-stop piggyback train between Chicago and Philadelphia. Family Lines has stated a new intermodal run between Hamlet, North Carolina, and Memphis, Tennessee, in an effort to provide faster service.

The shipper response under the deregulation of piggyback traffic has been quite favorable. Deregulation occurred at the end of March. Before then, piggyback traffic was down almost 6 percent from 1980. Since then, it is up 5 percent.

A petition is now pending before the Commission for the exemption of export coal. (Ex Parte No. 346, Sub-No. 7). The railroads involved believe that the exemption of export coal should improve the position of U.S. coal in the highly-competitive world markets and provide a more stable environment for railroad investments in equipment and facilities. Rail transportation is the only segment in the flow of U.S. export coal subject to economic regulation even though numerous railroads and water carriers compete for the same export sales.

The regulation of U.S. railroads is not only unfair but harmful to the ability of U.S. coals to compete in the world. Continued rate regulation is a significant impediment to the ability of the railroads to negotiate contracts as required by the export market. To the extent shippers believe they can obtain better rates through the regulatory process, the incentive to contract is lacking. On the other hand, the railroads' incentive to make the hugh investment necessary to meet the demands of an expanding export market is chilled if they are forced to rely for security on the vagaries of the regulatory process.

These vagaries arise because export shippers are unwilling to enter into a long-term contract with a rail carrier without a "regulatory backstop" clause assuring them of rates no higher than those their competitors are rquired to pay under Commission regulation. Thus, a rate bargained for is always subject to reduction because of regulatory action on a competing rate. This effectively nullifies the purpose of the contract provision in the Staggers Act. A contract under which the anticipated revenues can be reduced by regulatory action does not provide the assurance necessary for a large capital investment. It is highly unlikely that any of the other players in this market would make large investments on that basis and, given the competitive forces at work, neither should the railroads.

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[5] The railroads have sought clarification of whether antitrust protection still exists for per diem charges and certain rules and practices relating to the interchange of trailers and containers. A decision is still pending. There is, of course, no longer any immunity for the pricing of piggyback traffic.

JOINT RATES

The purpose of section 217, Compensatory Joint Rate Relief, was to provide a method whereby a carrier could, with a minimum of regulatory interference, get out of an uneconomic joint rate or route. Conrail viewed this as one of its most acute problems. Actions taken by Conrail and other railroads under this section have in some instances given rise to complaints by connecting carriers. In several instances litigation is pending. Because the views of the AAR members differ on the manner in which this section is being used, I will leave any expression of views to the members.

STATE CERTIFICATION

Section 214 was enacted "to ensure that the price and service flexibility and revenue adequacy goals of the Act are not undermined by state regulation of rates, practices, etc., which are not in accordance with these goals." (Conference Report at 106). Accordingly, state authority was preempted and a state was permitted to exercise economic regulation over an interstate railroad only if the Commission determined the state's standards and procedures were in accordance with federal standards and procedures.

The Act required the states to submit their standards and procedures for certification by January 29, 1981, and required the Commission to act within 90 days thereafter. To be candid, we must note that this provision has not been executed with the dispatch required by law. We do not say this to be overly critical. The statutory timetable was very short given the task to be accomplished both by the states and the Commission.

By the initial deadline of January 29, 1981, ten states[6] and the District of Columbia had failed to submit even the notice of an intent to comply originally required by the Commission. Accordingly, by the terms of the Act those states may not exercise jurisdiction over rail carriers.

The state responses under the initial deadline did not contain information sufficient to permit the Commission to issue certificates, especially in view of the fact that the certificates would have been valid for five years. Consequently, the Commission decided to issue provisional certificates which had the effect of permitting the states who had applied to continue exercising their jurisdiction. Concurrently, however, they were required to submit the information necessary to permit an informed decision with respect to their ability and willingness to comply with federal standards and procedures. Those submissions were originally due on June 29, 1981, but that date was extended to September 28, 1981. We assume that the Commission's action on the state applications will be forthcoming in the near future.

ABANDONMENTS

Section 402 of the Staggers Act made several amendments to existing law aimed principally at expediting the decisional process. That process seems to be working quite well.

A new element introduced into the abandonment process by the Staggers Act permits the Commission to require sale of a line to be abandoned by a railroad if the purchaser agrees to continue rail service over the line for at least two years. The price for the sale may not be set below the "fair market value" of the line. In a recent proceeding, the Commission set the price at the "net liquidation" value rather than at the fair market value of the property as part of an operating transportation corridor. The AAR believes this is clearly erroneous and has intervened in the appeal taken by the railroad involved. We assume the courts will agree with our construction of the statute so I do not believe it is a matter this Committee need concern itself with at the moment.

CARGO LIABILITY STUDY

Section 211 of the Staggers Act directed the Attorney General and the Interstate Commerce Commission within one year to independently investigate whether rail carriers should continue to be subject to section 11707 of title 49, United States Code, and submit a report to the Congress setting forth any recommendations for legislative action. The Commission filed its report on September 29, 1981. The Attorney General has not yet submitted his report.

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[6] Alaska, Arizona, California, Connecticut, Delaware, Hawaii, Massachusetts, Nevada, South Dakota, and Vermont.

Section 11707 embodies the so-called "Carmack Amendment" which provides strict liability for railroads with respect to loss or damage of freight. As the ten issues identified for study by section 211 suggest, the subject of cargo liability deserves a careful reevaluation. In completely rejecting the alternatives for a change and embracing the status quo, we believe the Commission report falls far short of the mark. We should also heartily disagree with two of the three specific legislative changes suggested by the Commission—the elimination of venue restrictions established by the Staggers Act and the award of attorney fees. We do not object to the third proposal, which would remove the $10,000 jurisdictional threshold for access to federal courts, inasmuch as it would encourage more uniform interpretation and application of the law.

We would urge the Committee to withhold consideration of the Commission's report pending receipt of the Attorney General's report. Hearings on both might then be in order.

SUMMATION

To sum up, Mr. Chairman, the railroad industry is generally satisfied with its experience to date under the Staggers Act. The rationale of the Act is sound and we remain convinced that it holds out the only hope for an econmically viable railroad industry. Based on our experience, there should be no lingering doubts that ironclad regulation simply will not work in a competitive environment.

To date, the Commission has moved with reasonable expedition to implment the Act and it has done so, by and large, in a manner that serves the basic purposes of the Act. The railroads still have a long way to go but, for the first time, we are in a position to build from a sound legislative base. We are very much concerned, however, that the twin objectives of the Act not be compromised. The forces of competition should continue to be substituted for the hand of government regulation wherever possible, and where regulation remains, it should be invoked in a manner that permits rather than thwards the attainment of adequate revenues.

We see two major threats on the horizon—the Commission's proposal to use fully allocated costs as the maximum rate standard and the hundreds of cases pending under the savings provision. The Commission's final resolution of these matters could well determine whether the "financial stability of the rail system of the United States"—the purpose sought by the Staggers Act—can be achieved.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR LONG AND THE ANSWERS THERETO

Question. We are told that the Commission has adopted the AAR index as the measure of cost escalation permitted by the Staggers Act expressly disregarding the offsetting impact of productivity upon actual costs. Am I correct in understanding that repeated application of this index can produce rates that exceed specific underlying costs by ever increasing percentages all immune from shipper challenge?

Answer. The AAR Index will not produce rates that exceed specific underlying costs by ever increasing percentages all immune from shipper challenge. In the first place, the Index, as a measure of rail cost inflation, will only increase faster than total costs when railroads are experiencing declines in traffic and/or when they experience increases in productivity. This is precisely what has happened during the first year of the Index, but it cannot continue indefinitely and, in fact, may reverse itself in future years. For example, because railroad carloadings have been on the decline and thus there is relatively less use of labor and certain other cost items, total costs have not been increasing quite as rapidly as unit costs—that is the cost per employee, gallons of fuel used, etc. Yet, if the decline in business continues, railroad earnings will be so adversely affected that rates could hardly be expected to rise. Conversely, when railroad business is on the rise, and there is a corresponding increase in the use of labor, fuel, and/or materials and supplies, total costs will increase at a greater rate than unit costs as measured by the AAR Index.

It is unfortunate that certain railroad adversaries confuse a shift in traffic consist with productivity. Because railroads have recently experienced an increase in coal traffic as opposed to declines in almost all other traffic, on the average each employee is producing more ton-miles. Yet, these employees are not necessarily more productive as all railroad employees do not produce ton-miles. In fact, where the railroads substitute higher-rated traffic (general merchandise) with lower-rated traffic (coal), "real" earnings may decline.

Where a gain in productivity does result, in the short run the Index may outpace total costs; however, as long as railroads are revenue inadequate, they should reap the benefits of such gains. After all, to penalize railroads that are revenue inadequate by taking away their productivity gains is really a shippers' penalty. This would prolong the achievement of revenue adequacy and possibly result in less than adequate railroad investments in plant and other equipment. Also, a downward adjustment in the Index for productivity gains would mean that where the railroads were unproductive, an upward adjustment would also be made. Thus, both railroads and shippers would be penalized for both increasing and decreasing railroad productivity.

Finally, it is important to note that changes in the AAR Index are not necessarily changes in the level of rates. The Index serves as the maximum level of uncontested rate adjustments and because of intense competition, many railroad rates are not adjusted in accordance with changes in the Index. In fact, many railroads have reduced freight rates even in the face of increases in total, and unit costs.

Question. Do you agree that any differential pricing of captive traffic should be limited to a railroad that demonstrates a diligent program to minimize revenue shortfall from other traffic and further demonstrates that any differential pricing is spread equitably.

Answer. Differential pricing is an equitable system for all shippers. On one hand, shippers with lower revenue-cost ratios are enjoying railroad service which they could not afford at higher rates. On the other hand, shippers with higher revenue-cost ratios are paying less than they would have if the shippers on the low end of the scale were not using the railroad. Thus, the only case where differential pricing is inequitable is where some shippers are charged rates which are below marginal costs—a phenomenon which not only results in no contribution to overhead, but actually results in financial loss. Obviously, it is not in the interest of any railroad to maintain such rates and to the extent they exist railroads are working diligently to eliminate them. In the past, many were maintained at below cost levels because the regulatory systems (federal and state) required them to be. The Staggers Act tried to reduce many of those impediments.

Question. At the time the 4-R Act concept of revenue adequacy was further implemented in The Staggers Act, the Commission had found thirteen Class I railroads to be revenue adequate including such major carriers as Norfolk & Western, Southern, Union Pacific, Missouri Pacific, Denver & Rio Grande Western and Chesapeake & Ohio. I am advised that in the most recent determination of revenue adequacy none of the carriers that I've named have been found by the Commission to be earning adequate revenues. Are these railroads that I have named earning more or less than they were at the time the Act was passed?

Answer. Some of the named railroads are earning more than they were at the time the Staggers Act was passed, but because the ICC has now developed a more appropriate standard for determining revenue adequacy, they are no longer revenue adequate. The principal reason for the ICC's modification had little to do with the Staggers Act.

In the ICC's prior determination, thirteen railroads were found to meet some of the tests for revenue adequacy because they satisfied certain financial tests originally established by the ICC which were unexplained and unfounded in sound financial theory—a deficiency which upon reconsideration, the ICC corrected. Currently, a basic objective test is used by the ICC to determine revenue adequacy; namely, a railroad's return on investment must at least equal its cost of capital. In 1980, only the Clinchfield, the Fort Worth and Denver, and the Pittsburgh and Lake Erie achieved that level (then 12.1 percent).

A direct comparison of the present earnings of the named railroads to their earnings at the time that the Staggers Act was passed is not possible. Earnings during 1980, included only three months of post Staggers Act revenue, and earnings for 1981 are not yet available. One possible comparison, although limited, is to compare the first nine months of 1980 earnings to the first nine months of 1981 earnings.

	Net railway operating income	
	3d 1980 YTD	3d 1981 YTD
Norfolk & Western	$131,504,000	164,727,000
Southern	157,385,000	175,423,000
Union Pacific	161,518,000	167,271,000

	Net railway operating income	
	3d 1980 YTD	3d 1981 YTD
Missouri Pacific	122,670,000	137,269,000
Denver Rio Grande	20,806,000	20,200,000
Chesapeake & Ohio	52,877,000	30,344,000

Although some increases appear substantial, one must consider four facts. First, these are nominal dollar amounts and are not measured relative to a net investment base or adjusted for inflation. Second, the findings of the Staggers Act detailed that the earnings of the railroads were the lowest of any transportation mode; and, the Act set as a goal "to reform Federal regulatory policy to preserve a safe, adequate, economical, efficient, and financially stable rail system." Thus, higher earnings are one of the intents of the Staggers Act. Third, a two-year comparison of earnings is subject to volatility resulting from changes in the overall economy. And fourth, since the Staggers Act has not been fully implemented, rail rates will continue to change due to less regulation and increased competition, so that revenue may not increase at the same rate in future years. Unless earnings continue to increase, these and other railroads cannot hope to achieve revenue adequacy—which of course, is the principal purpose of the Staggers Act.

Question. Do you feel that Congress should go ahead and fund the Railroad Accounting Principles Board?

Answer. No. It appears unnecessary to fund the Railroad Accounting Principles Board (RAPB) at this time. The main objective of the RAPB is to establish principles governing the determination of economically-accurate railroad costs associated with movements of goods. The Interstate Commerce Commission (ICC), in cooperation with the railroad industry and shippers, is presently developing a Uniform Rail Costing System (URCS). Since URCS will meet most of the requirements of the RAPB, the ICC agreed to take over the responsibility of the RAPB in developing these principles. The development of URCS has been under way for over three years and is near completion. In addition, the ICC has agreed to perform the remaining requirements of the RAPB by reviewing the broad accounting principles applicable to the railroads.

Question. Are railroad holding companies adequately reinvesting revenues in the rail system?

Answer. Yes. Railroad holding companies are more than adequately reinvesting in the rail plant.

In 1980, over 70 percent of the revenues and total assets of Class I railroads were controlled by holding companies. However, only IC Industries, Union Pacific, US Steel, and Katy Industries were truly diversified holding companies (less than 70 percent of revenues come from railroad operations).

Charges are often made that railroad holding companies are not properly reinvesting railroad earnings. Such charges are fallacious. During 1980, holding-company owned Class I railroads spent $2.9 billion (2.5 times their ordinary income) on railroad capital expenditures. From 1971 to 1980, rail capital outlays exceeded $20 billion while ordinary income was only $5.7 billion. In a period during which return on investment averaged two percent, the railroad holding companies' record of reinvestment is commendable.

During the past ten years, studies have identified capital requirements far in excess of actual spending. As railroads increase their revenues through the techniques provided in the Staggers Act of 1980, capital expenditures by railroads and their holding companies will increase.

Question. Do you feel it is proper for railroads to abandon profitable branchlines, even if they invest the money in non-railroad ventures?

Answer. Profitable branchlines will not be abandoned.

A profitable branchline must be defined as Light-Density-Line (LDL) which earns, in addition to the full costs of operations, an adequate return on the net investment in plant and equipment. To our knowledge, railroads are not abandoning profitable LDL lines nor would they have any incentive for doing so. Since few carriers are earning an adequate rate of return on their total rail plant, it would be irrational to abandon a line which was providing adequate returns. Where a line fails to cover "avoidable costs" (the expenses that would not be incurred were the line abandoned) plus the cost of capital invested in the line, the Staggers Act does provide a remedy short of abandonment. Any interested person can require continued operation if it is willing to provide financial assistance sufficient to cover the loss being sustained by the carrier. If the line in question does cover avoidable costs, the ICC will deny such

applications. Obviously, the railroads have little incentive to pay for the high costs of processing such applications.

Investment in non-railroad activities would actually be encouraged by requiring a railroad to operate unprofitable lines and by limiting a railroad's return below levels available in other industries. If returns are maintained at low levels due to regulation, investors, who cannot be regulated, will require management to reinvest the funds into profitable industries. The only mechanism that guarantees reinvestment in a regulated industry is the prospect that the firm will have the opportunity to earn income at levels comparable to unregulated firms.

Question. Certain railroad presidents (Claytor of N&W and Hall of Southern) have stated that by the 1990's only six giant corporations will control the U.S. rail system. Do you agree with this assessment? If it does happen, will it be good or bad?

Answer. Today, there are nine railroad systems with annual freight revenues in excess of $1 billion. If the currently pending mergers are consummated, that number will be reduced to seven. Should any other large merger be proposed, its approval would be contingent upon a finding by the ICC that it was in the public interest. Absent the kind of inquiry the Commission would have to make in reaching that judgment, I am not in a position to say whether additional particular mergers would be good or bad.

Senator DANFORTH. Thank you very much, Mr. Dempsey.

Our next witnesses are a panel: James A. Hagen, Henry Allyn, and Curtis J. Hockaday—the carrier panel.

STATEMENTS OF JAMES A. HAGEN, SR., VICE PRESIDENT FOR MARKETING AND SALES, CONRAIL; HENRY G. ALLYN, PRESIDENT, PITTSBURGH & LAKE ERIE RAILROAD; AND CURTIS J. HOCKADAY, PRESIDENT, GREEN BAY & WESTERN RAILROAD

Mr. HAGEN. Thank you, Mr. Chairman.

My prepared remarks explain some of the positive things that the Staggers Act has done to improve rail ratemaking, and my prepared remarks also discuss some of the more difficult but also more innovative things that Conrail has done to impact on its deficit.

I think the single point that I want to stress today is that all these activities will amount to nothing if the railroads are not permitted to earn adequate revenues. That's something, as Mr. Dempsey pointed out, that we're not doing today.

The ICC has proposed a system of maximum ratemaking which will diminish Conrail's already inadequate revenue by an additional $300 million a year. If these rate ceilings are applied, Conrail and many other railroads in the country are going to end up wards of the State. And the fact is that the adequate revenue standard of the Staggers Act has not been given the complete attention that is demanded by the statute.

We are hopeful that the ICC would recognize this fact in the coming months.

The cardinal fact of railroad marketing is that differential pricing is necessary. Differential pricing means that different shippers must pay different profit margins to the railroads, but all rates must cover variable costs. But some must contribute to overhead more than others. The reason for this is that some parts of the railroad traffic base are extremely competitive, and some are less so.

All shippers say that they do not want to cross-subsidize other traffic, and they are quite right, but ending cross-subsidies is not the same thing as saying that coal shippers should not bear more of the rail overhead than other traffic. If the other traffic went away, the coal shipper would have to bear a still larger share.

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The stark fact is that if the ICC and the interest groups among the shippers impose a standard of maximum rates that's too low, the railroads will have no choice but to drive off their competitive boxcar and piggyback traffic, forcing coal rates even higher. So, for this reason, differential pricing is essential if the system is to survive.

Section 229 of the Staggers Act also invited shippers to bring complaints that they thought their rates were too high. More than 800 such complaints were filed; over one-quarter of these affect Conrail. The burden of defending these complaints is enormously disruptive to our marketing effort, and will become increasingly so in the future.

The consequence of even modest relief to shippers would be devastating to Conrail, which is just now beginning to rise to its knees. Only if the ICC is willing to take a new approach to rate regulation is there hope that Conrail and other railroads can become self-sufficient and competitive in the capital market.

For example, Conrail has sought deregulation of boxcar traffic, a highly competitive kind of traffic which we are losing to trucks. We filed our position in May of 1981 and 5 months later we are still waiting to see what the Commission will do. So, we feel that we need prompt action if the boxcar business is to survive.

Another area where a new approach is needed is the "hunting season" case and the various coal rate proceedings.

As long as the Commission tries to relate rate ceilings to costs instead of market conditions, the carriers will have no incentive to reduce their costs for efficiency. The new Commission has a chance to change the situation. Otherwise, Conrail's efforts to save itself will be turned back.

I am pleased to hear the Chairman of the ICC's remarks that they have all these things under consideration, and I am happy to be here to present my views.

[The statement follows.]

Statement of James A. Hagen, Senior Vice President—Marketing and Sales, Consolidated Rail Corporation

A year ago, Conrail greeted the Staggers Rail Act of 1980 with great optimism. As we saw it, the Act presented an opportunity which, if skillfully administered by the ICC, could enable Conrail to at least begin to address the problems which faced it. Now, a year later, we are not so sure. The ICC has indeed taken some beneficial first steps. But unless it moves far more boldly—particularly in the area of adequate revenue—the gains promised by the Staggers Act will be illusory. Without adequate revenue, the rail industry as a whole, and Conrail with it, will continue a long term decline.

When it was passed, many viewed the Staggers Act as "deregulation." It was not that. What the Staggers Act did was give the ICC discretion to deregulate the railroads selectively—or not—in much the way the Commission saw fit. During the past year the Commission has made some steps which have enabled the railroads, and Conrail, to cure some of their most egregious problems. But, at the same time, the Commission has suggested that it will take novel and unwarranted measures in the area of maximum rate regulation which will prevent the industry from ever achieving revenue adequacy.

Let me start by talking about some of the good things that Conrail has been able to do under the Staggers Act. Then I can get into some of our worries about how the broader purposes of the Staggers Act may not be fulfilled for the future.

Conrail has just completed two consecutive profitable quarters. The profits for the third quarter of this year were higher than for any quarter since Conrail's formation, and there is an excellent chance that we shall break even or better for the year 1981. Last spring Conrail negotiated a $200 million annual labor saving propos-

al with its unions, and all but a handful of the unions have ratified that agreement. This summer you helped pass the Northeast Rail Service Act of 1981, a statute which cured several of the deficiencies of the Staggers Act. The new law addressed the issues of funding, excess employees, commuter service, and the especially sensitive issue of line abandonments. And in June Conrail won *Modern Railroads* magazine's Golden Freight Car Awards for the second year in a row in recognition of our marketing effort. But we still have a long way to go before Conrail can attract capital to improve its operations further.

As far as the Staggers Act is concerned, one of the most significant benefits to us has been in the zone of rate flexibility provisions. Using those provisions, the Commission has developed an inflaton index. (The Commission chose not to use other provisions of the Staggers Act which provide more specifically for an inflation recovery index, but to date the workings of the procedure chosen by the Commission have been entirely satisfactory). For the past three quarters, the railroads have been able to use the new index to recover inflation related costs in their joint line rates. The new procedures do away with the dilatory and wasteful proceedings that previously resulted in an ever-increasing inflation shortfall. The beneficial effect of the inflation indexing procedure is best understood when it is recognized that most of the railroads' ratemaking efforts can now be devoted to *reducing* rates selectively below the index levels. Thus the aggregate structure does not rise as fast as the index, but the railroads now can focus their attention on individual rates, as I believe is proper.

A second useful development has been Staggers Act's formal pronouncement that contract rates are lawful. In the period since the Staggers Act was passed, Conrail has published 24 contract rates covering broad diversity of commodities. Many of these contracts contain special service obligations, such as improved car supply, better transit times, or more reliable service. These benefits are perceived as desirable by both Conrail and its customers, yet were for years forbidden.

Finally, the surcharge and joint rate cancellation provisions of the Act have been used by Conrail. We have published 34 surcharges, which would have the potential to produce about $21.9 annually if no diversion were to occur. This is added revenue on traffic that has been chronically money-losing because of divisions imbalances. We also have used provisions of the Staggers Act, as well as the old law, to cancel joint rates on inefficient routes. In so doing we have addressed some of the ill-effects of the interterritorial rail mergers which surround us and some of the distortions caused by the ICC's long out-of-date prescription of interterritorial divisions.

Perhaps the most important effect of the surcharge and route closing provisions of the Staggers Act is the way in which they affect railroad costs. Surcharges typically are published at a high level to cover costs on routes where deficits are the greatest. (The statutory procedures require equal surcharges for all routes, at least initially). Then the surcharges are rolled back selectively on routes where costs are lower. The result is that the lowest rates are available to shippers on the most efficient routes. Traffic which had formerly been dispersed over a multiplicity of routes is focused on the best. As a result, there often is very little cost increase to shippers and a significant cost reduction to the carriers. This in my view has been a contributing factor to Conrail's improved economic performance in 1981 and will continue to contribute to improvements in the future.

A side benefit to the surcharge statute is that it leads to ratemaking negotiations that often avoid the need for further surcharges. Since the Staggers Act was passed, we have experienced a new willingness on the part of other carriers to agree to both rate levels and divisions changes that were unheard of before the Staggers Act.

These initial actions, however, should not lead to euphoria. They produce benefits measured in the tens of millions of dollars. But the problem can be measured in the hundreds of millions. Some of the larger questions remain unresolved, and only significant efforts—and a change of direction—by the ICC can make the necessary changes happen. The problem is one of *procedure* controlling *substance*. The Commission has always bent over backwards to give parties "their day in court" or to adhere to "the letter of the law." But there is no physical way that the Commission or any other tribunal can handle the volume of individual rate cases that would be necessary under traditional procedures if the carriers are to achieve revenue adequacy. And revenue adequacy is a crucial goal of the Staggers Act. What has happened is that the " letter" of the Interstate Commerce Act is being used to thwart attainment of the explicit goals of the Staggers Act. Only if *broad* approaches are adopted by the Commission will any motion at all be possible.

As one example, Conrail has asked the ICC to deregulate boxcar traffic. Boxcar traffic in the Northeast has been chronically unprofitable. Because of this, many persons have said that Conrail is trying to get out of the business—and if there are not changes in the present system of regulation those people will surely be right.

The fact is that boxcar traffic is highly truck competitive. Yet, unlike the trucks, boxcars generally return to the origin empty, where utilization is poor. Moreover the rent for boxcars paid to other railroads, something prescribed by the ICC, tends to be very high, even in time when there is a surplus. These factors drive up boxcar rates and drive the business to the trucks.

To address these problems Conrail has asked the ICC to deregulate boxcar traffic. This would mean that rates and service and carhire could all be tailored to demand. Conrail would not have to handle boxcar traffic unless it could make money on it. But we think it could make money on a great deal of such traffic, and shippers would benefit.

Conrail filed its petition for deregulation with the ICC on May 22, 1981. Five months later, we are still awaiting action. We think that prompt action is important if Conrail is to be able to stem boxcar losses that exceed $100 million a year on and to interline traffic alone avoid the consequent burden on other shippers. The Staggers Act provides the remedy, but the ICC needs to have the courage to use that remedy.

Another opportunity which has not yet been seized is presented by the rate bureau changes of the Staggers Act. Those changes require single line rates to be made separately from joint line rates. They require joint line rates to be made separately as between competitors. The underlying purpose appears to have been to break up the monolithic rate structure and require the railroads to compete one against another.

We believe that these changes will be highly beneficial both to the rail industry and to shippers because they will force the carriers to accept traffic over the most efficient routes and to keep their rates at the lowest possible level in order to compete. Under the old system, rates were maintained at artificially high levels in order to protect the needs of inefficient carriers and operations over inefficient routes. We believe that in many markets Conrail will be the most efficient carrier, will price its services competitively, and will be able to earn an adequate profit on its overall operations.

The way to do this is through a system of what rate men call "proportional rates." With proportional rates, shippers calculate charges for their through movement by adding together separate factors for each carrier over which the shipment passes. The rates are different for different routes, unlike the present system; and where the costs are lower, the rates are lower. Tariffs can be greatly simplified. Conrail has already published such proportional rates on recyclable materials and grain, and the reception of most of our customers has been enthusiastic. For the most part, only our connecting carriers have opposed us. The ICC so far has seen things our way and we are hopeful that we shall prevail when the matter is finally decided.

There are some very real storm clouds building, however. At a time when the railroad industry needs hundreds of millions of dollars more if the existing plant is to be rebuilt and shippers are to be well served (and the need exists for virtually all railroads, not just Conrail), the Commission has proposed rate regulation methods that could *take away* money the railroads now have. These methods would limit the railroads to "fully allocated costs" as a ceiling for prices. The proposals are being advanced by the Commission in various coal rate proceedings and will bear directly upon the roughly 700 "hunting season" cases that have arisen under Section 229 of the Staggers Act.

The hunting season cases are a dramatic example of the failure of litigation. Conrail is involved in more than 200 cases, and the discovery against us in just *one* of those cases will take 270 man-days to answer if not withdrawn. The very existence of that litigation—encouraged by the Staggers Act—threatens our ongoing ability to do business.

Part of the error by the Commission which gave rise to those cases is its novel and ill-conceived effort to relate maximum rates to cost levels. Where rate ceilings are tied to costs, there is no incentive to reduce costs or operate efficiently. Cost-based ratemaking means that the carriers cannot retain the benefits of doing what they can do well. And until the carriers are attracting revenue that is adequate for their survival, such regulation is both misguided and contrary to the goals of the Staggers Act.

The cardinal fact of railroad marketing is that differential pricing is a necessity. Differential pricing means that different shippers must provide different profit margins to the railroad. All rates must cover variable costs, but some must contribute more toward overhead than others. The reason for this is that some parts of the railroad traffic base are competitive, and others are not.

Coal shippers say that they do not want to cross-subsidize other traffic. And they are quite right. They should not have to. But that is not the same as saying that

they should bear no more of the railroad's overhead than other traffic, because if the other traffic went away the coal shippers would have to bear a larger share. Competitively restrained traffic like boxcar traffic and piggyback traffic simply cannot suffer significant rate increases or much of it will be diverted to trucks. That traffic does contribute to overhead costs—lightening the burden on coal shippers—but it moves at prices far below fully allocated costs. The only way that total costs can be covered is to have other traffic, such as coal, return more than fully allocated cost. For this reason, differential pricing, something that the ICC has recently repudiated, is essential if the carriers are to survive.

I view this problem with an enormous amount of concern. In my career, I have been President of the United States Railway Association and a Vice President of Southern Railway, in addition to other railroad jobs. I have observed that the revenues of the industry are simply not adequate. The current proposals of the ICC to *diminish* those revenues will be devastating. At Conrail, we estimate that the new ICC pricing system would reduce Conrail revenues by well over $300 million a year, if fully applied (and competition would quickly cause it to be fully applied). For these reasons, the Commission must allow the railroads to adhere to the economically sound principle of differential pricing in order if they are ever to achieve the adequate revenues which the Staggers Act calls for.

In conclusion, I view the future with doubt. Conrail has made great strides in cutting costs and getting its own house in order. The Staggers Act has helped us in some ways, and it holds the promise for helping us in others. But the Commission has embarked on a course of maximum rate regulation that could put Conrail and most other railroads on the federal dole permanently. Only if the Commission is willing to view adequate revenues with the same receptiveness that it has viewed the other opportunities of the Staggers Act will the railroads be able to avoid further decay.

Senator DANFORTH. Mr. Allyn?

Mr. ALLYN. Thank you, Mr. Chairman. At the outset, I would like to correct a misinterpretation that came out in the figures that Bill Dempsey quoted about profitable railroads. We happen to be a small, profitable railroad, and have been for years. We operate in western Pennsylvania and eastern Ohio, and we are one of the three that he indicated exceeded the profit standard of the ICC, but it's an accounting aberration. I wish, indeed, it were true. I think it came out at 17.8 percent. That is purely because the railroad was sold by Penn Central in May of 1979. The accounting industry required us to adopt "purchase accounting." On an historical basis, equivalent to other railroads' standards, it would have been 4.4 percent. I wish it could be the former!

We support the general intention of the Staggers Act as my submitted testimony indicates. I think railroads, too, have to be free, and they now are, to differentially price their services.

We do feel, however, that there are needs for revision in the act, and in particular, being a line that is very heavily involved in connecting traffic, that the proponent carrier of a joint route cancellation should bear the brunt of the defense of the economics of that decision. As the act is now drawn, it throws the burden upon the other members of the joint group to disprove the allegations, or assertions, if you will, of the proponent line. I think if that particular matter is adjusted so that the proponent—who, after all, has all the facts at his disposal—bears the brunt of that proof, it would be in line with national transportation policy, and certainly would improve competitive opportunity for the shippers.

That's all I have to say, Mr. Chairman.

[The statement follows:]

Statement of Henry G. Allyn, Jr., President and Chief Executive Officer, Pittsburgh & Lake Erie Railroad Co.

Mr. Chairman and members of the subcommittee, thank you for the opportunity to appear before you this morning to share with you some views held by The Pittsburgh & Lake Erie Railroad Company (P&LE) regarding improvements to the Staggers Act which will strengthen competitive rail transportation. First, let me give you a few brief facts concerning the P&LE.

The P&LE is a small Class I railroad, principally engaged in providing freight service over 345 miles of main line, serving southwestern Pennsylvania and northeastern Ohio. Our main lines extend north from a junction at Connellsville, Pennsylvania, with the Chessie, and at Brownsville, Pennsylvania, with the Monongahela Railway. These lines join at McKeesport and extend north through Pittsburgh, Aliquippa and Beaver Falls to Youngstown, Ohio, and from there north via trackage rights over Conrail to iron ore and coal docks and a connection with the Norfolk & Western Railway at Ashtabula, Ohio. In addition, we operate with trackage rights over the former Erie Lackawanna (now Conrail) from Youngstown east through Sharon, Pennsylvania to a connection with the Bessemer & Lake Erie Railroad near Greenville, Pennsylvania. A map of the P&LE system is attached for reference.

P&LE has had a corporate existence and been profitably operated for more than 100 years. For many years, it was a corporate subsidiary of the New York Central System and later Penn Central Transportation Company. As a result of Congressional action, P&LE was excluded from the rail properties which Penn Central conveyed to Conrail in 1976. In 1979, Penn Central sold the railroad to a privately owned holding company now known as Pleco Inc. Its headquarters remain in Pittsburgh, Pennsylvania and normally employs 2300 people.

For many years, a distinguishing feature of the P&LE has been its relatively large fleet of freight cars. Of all the railroads operating within the Northeast, the size of the P&LE's car fleet ranks fourth behind Chessie, Conrail and N&W. On Sepetember 2, 1981, the P&LE owned, leased and operated 17,332 freight cars of various types. P&LE's commitment to its freight customers and to its large car fleet was reenforced in 1979–1980 when it acquired 2,750 new freight cars having a total value of over $100 million and today we are waiting delivery of an additional 400 new cars.

P&LE taffic consists primarily of bulk volumes of coal, coke, iron ore, and semi-finished iron and steel products. A smaller portion (perhaps 25 percent) of or business involves a wide variety of industrial products for shippers, both large and small. Such traffic is nevertheless important to the P&LE in terms of the revenues it provides. During the poor traffic year of 1980, P&LE received total revenues of $83 million for handling 270,000 carloads of freight. Thirty percent of that amount was local business which originated and terminated on P&LE lines, and 70 percent involved interline business with other railroads, mainly Conrail, N&W and the Chessie System. Therefore, over two-thirds of our traffic involve handling with other carriers.

The volume of traffic interchanged with Conrail is especially valuable to the P&LE. The large extent to which P&LE interchanges traffic with Conrail reflects not only the historical fact that the P&LE had been affiliated for many years with Conrail's predecessors, the New York Central and later Penn Central, but also that Conrail, a combination of six eastern railroads, serves most of the shipping points within the Northeast which are important to P&LE's customers. As an indication of the importance of Conrail to P&LE, is the fact that in 1979 we interchanged about 110,000 carloads of our freight with them at Youngstown, Ohio. As such, the volume of that interchange ranked seventh in the entire nation. In the same year, P&LE and Conrail interchange an additional 21,000 carloads of freight at other junctions. In terms of revenues, P&LE received over $32 million for shipments which it handled jointly with Conrail 1979, while Conrail received close to $89 million as its share for handling the same business. Conrail received more in interline revenues from P&LE traffic that year then it received from many other larger railroads such as the Chicago and North Western, Illionois Central Gulf, Canadian National and the Canadian Pacific—Soo Lines.

Similarly, P&LE interchanges a large volume of traffic with the N&W at Ashtabula. In 1979, P&LE and the N&W exchanged approximately 24,700 carloads of freight there. That traffic also produces a significant revenue for the P&LE. The P&LE also interchanges important volumes with the Chessie and Bessemer and Lake Erie.

It is very important to note that while P&LE interchanges large volumes of traffic with these major connecting carriers, these same lines simultaneously operate competing lines which can be and are continuously used to short haul the P&LE or

reach many P&LE points directly. As a small Class I railroad, P&LE is particularly concerned that certain provisions in the Staggers Act are being used, principally by Conrail, in an effort to impede rather than promote rail competition.

P&LE supports deregulation and the competitive national rail transportation policy enunciated in the Staggers Act. However, in several very technical provisions of the Staggers Act, changes were enacted which P&LE believes permits the larger Class I railroads to exercise their market power so as to preclude effective intervention by the ICC which might otherwise preserve the competitive rail service. The most crucial problem area involves the shift in the burden of proof to a challenger of a joint line rate or route cancellation.

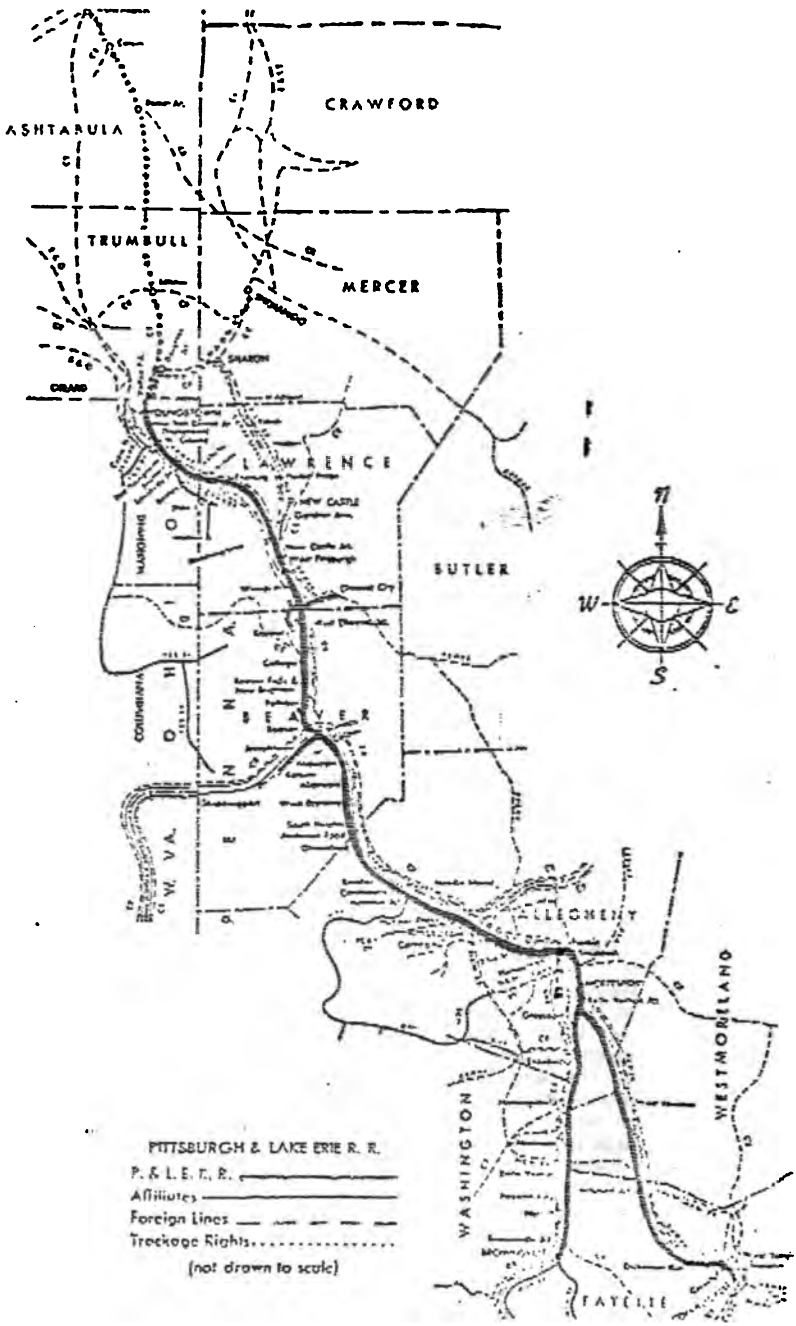
Under the surcharge provision of 49 U.S.C. § 10705(a), Congress developed an effective, albeit complicated procedure for using rate differentials to attract traffic to the least costly, most efficient joint routes. The surcharge provision, however, does not necessarily eliminate higher cost, competing joint routes. A shipper may still choose to use such a route and the participating carriers will certainly solicit traffic for those routes. The surcharge provision was enacted almost exclusively for the benefit of Conrail. But Conrail today is not willing to settle for joint routes on which it can earn only 110 percent of variable cost. Instead, it has involved the rate cancellation provisions of Section 10705(a)(c) which permits a carrier to unilaterally cancel the application of a joint rate to a through joint route unless another participating carrier in that route demonstrates to the ICC that the cancelling carrier's share in the revenue under the joint rate is equal to or greater than 110 percent of the cancelling carrier's variable cost of providing that service. Conrail recently cancelled numerous joint rates with northeastern railroads and, in effect, told its connections that unless they could prove that Conrail's revenues exceeded the 110-percent level, Conrail would simply refuse to deal with them.

This action was aggrevated even further by the increased burden placed on a protestant to a rate cancellation under the provisions of 49 U.S.C. § 10107(c), which no longer provides any real opportunity for ICC suspension of a rate cancellation. Under the standards of Section 10707 (c) and (d), there is virtually no evidentiary showing that can be developed by Conrail's connecting carriers in the very short period provided under the ICC's Rules of Procedure which can establish that they are "substantially likely" to prevail on the merits and are, therefore, entitled to a suspension of Conrail's rate cancellation.

While litigation ensues at the ICC and through the appellate courts, those joint rates stay cancelled and Conrail will make every effort to secure its grip on traffic which had previously moved over those routes. Conrail has cavalierly forced its connecting carriers to prove that Conrail makes at least 110 percent of its variable costs on a multitude of joint routes, and in the meanwhile acquires an even greater share of the market, much of which it already dominates, at the expense of its connections.

It is manifestly ridiculous to expect that other railroads can promptly analyze and respond with a route by route rebuttal of Conrail's numerous rate cancellations. It is simple justice that he who has best access to the evidence should bear the burden of proof. Conrail is in a far better position to know which of its joint rates over which specific through routes exceed the 110-percent standard. If any carrier wishes to cancel a joint rate, it is only fair that it come forward prepared to justify the cancellation rather than impose that burden on a connecting carrier. Time could be saved and expensive litigation would thus be avoided. There would also be less temptation to use the Staggers Act as a market weapon against one's rail competitors. Shippers could retain the benefit of alternative routings albeit with different price levels and our national transportation policy would be far better served.

Sincerely, I urge this Committee to place the evidentiary burdens of a joint rate cancellation on the proponent carrier where they rightly belong. I will be delighted to respond to any questions this Committee may have.



ASHTABULA
CRAWFORD
TRUMBULL
MERCER
LAWRENCE
NEW CASTLE
BUTLER
BEAVER
COLUMBIANA
W. VA.
ALLEGHENY
WESTMORELAND
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S
PITTSBURGH & LAKE ERIE R. R.
P. & L. E. R. R.
Affiliates
Foreign Lines
Trackage Rights
(not drawn to scale)

Senator DANFORTH. Thank you, sir.

Mr. Hockaday?

Mr. HOCKADAY. Thank you. I appreciate the opportunity to be here to testify before your committee. The goals of the Staggers Act were intended to increase competition; to maintain the balance of power between shippers, carriers, and the public need; to prevent undue concentration of market power; and avoid predatory pricing and discrimination.

Section 217 of the recancellation and surcharge is being misused by some of the major carriers to cancel routes from smaller carriers. Under litigation—Conrail, Burlington Northern, and Union Pacific is canceling routes unduly. This threatens the survival of my company and other smaller carriers.

Even more prevalent occurrences—one that hasn't come to the attention of the ICC and this committee—and that is on a day-to-day basis, these lines are refusing to place Green Bay and Western and other carriers on their routes on all new reduced rates that were established in market competition. This simply ties our hands. It does not allow us to compete. Being in the route guarantees us no traffic. And what we need, very simply, is the right to compete.

Thank you.

[The complete statement follows:]

STATEMENT OF CURTIS J. HOCKADAY, PRESIDENT, GREEN BAY & WESTERN RAILROAD CO.

My name Curtis J. Hockaday, and I am President of the Green Bay and Western Railroad Company (GB&W). The GB&W is a Class II railroad with 250 miles of main line track providing service in an East-West direction between Winona, Minnesota, on the West and Kewaunee, Wisconsin, on the East. The purpose of my testimony is to point out for the Committee where certain sections of the Staggers Rail Act of 1980 have been helpful and perhaps more importantly, the manner of misuse of the positive nature and intent of certain provisions which have been and will continue to be harmful to the GB&W and our shippers and the communities we serve.

The 1980 Staggers Act was a dramatic peice of legislation for the rail industry and our customers. The change in policy set forth in Public Law 96-448 was so revolutionary, reaction by shipppers and carriers implementing various provisions was cautious to the point of non-use or non-application for many months. As a result, the full impact may not be determined for several years.

One of the most instructive writing occurs in Sec. 3 and Sec. 101(a). Section 10101a whereby Congress set forth most flexible positive goals stressing competition as the theme. Those provisions fully outline the Nation's rail transportation policy designed to foster a sound competitive transportation system balancing the needs of the carriers, shippers, and the public.

Other good, positive provisions include:

Sec. 203 Section 10707a permitting quarterly rate adjustments directly offsetting rail cost increases. This is excellent as carriers have experienced shortfall on ex partes for years.

Sec. 206 Section 10712 allowing the Commission to prescribe a percentage rate increase or rate index in order to compensate for inflationary cost increases. This also measurably assists carriers to maintain a pace in the business world.

Sec. 208 Section 10713 permits transportation contracts. This is an outstanding marketing tool enabling a customer and carrier to negotiate for legally binding charges, services, and market share on a mutually beneficial basis.

There are numerous other sections which serve to balance the needs of carriers, shippers, and the public; however, I suspect the Committee is fully apprised of the positive aspects of the Staggers Act. It is the abuse of the goals and intent of the Act and flagrant misuse of the provisions that are of major concern to the GB&W and numerous other carriers.

Sec. 217(a)(1) Section 10705a authorizes joint rate surcharges and cancellations, and several carriers are using this provision in a manner injurious to the GB&W and other similarly situated railroads. Of great importance to this Committee is the fact that this extraordinary provision is being misued in a way never contemplated by Congress at the time of passage.

In order to explain my use of the term "extraordinary," it may be useful to briefly review the events which culminated with inclusion of Section 217 as a part of the Staggers Rail Act of 1980.[1]

In the early consideration of the need for legislation deregulating railroads, Conrail contended that one of its major problems was the inability to extricate itself from specific joint rates it had identified with other carriers where Conrail claimed it was not receiving revenues that were above its variable costs. They were successful in convincing the Department of Transportation in this regard, and the deregulation bill initially proposed by the Administration would have granted Conrail (and other railroads) a broad and almost unrestricted right to cancel or place surcharges on joint rates.[2] This pervasive provision was opposed by virtually all other railroads as well as by shippers and was not included in later versions of the bill. Toward the end of its legislative consideration, that provision, substantially modified, was put back in the bill when one of its foremost opponents, Southern Railway, agreed with Conrail on a carefully circumscribed compromise provision.

While that compromise provision was acceptable to Southern Railway (which had and has the economic strength to protect itself) it was ardently opposed by numerous other railroads, particularly small and mid-size railroads, i.e. those which lacked substantive economic strength. This included the GB&W. As a result of that opposition, some safeguards were included in the joint rate provision specifically to protect small and mid-size railroads.

Unfortunately, those limited safeguards are proving to be little more than tokens. For the most part, Conrail is ignoring them and the Commission thus far has not taken an aggressive stance to ensure that they are implemented effectively in providing the protection which was intended.

One of the most disturbing aspects of Conrail's behavior is its treatment of the section not as a limited provision by which a specific joint rate may be cancelled or surcharged but as a broad nonrestricted provision under which large numbers of unspecified joint rates via numerous routes and gateways may be cancelled or subjected to surcharges.

Conrail's contention at the time they promoted enactment of the joint rate provision was that they had identified a number of specific joint rates which failed to return them revenues exceeding their variable cost. Notwithstanding that contention, Conrail now uses the provision in a shotgun fashion not directed to specific joint rates but directed to a large number of unidentified joint rates via certain shorthaul gateways and connections.

A prime example of this is their proposal to close routes and gateways through the process of amending the Eastern Railroads' routing guide (TEA Routing Guide).[3] While that action clearly proposes to close routes, Conrail insists that the action is in reality the cancellation of specific joint rates. Of great importance to the GB&W is that the Conrail action would close one of its two available connections to Eastern destinations, i.e. its Chessie connection to Conrail destinations and points beyond Conrail.

Conrail's justification for this action is that the changes proposed in the TEA Routing Guide Tariff would still leave one Eastern connection available to GB&W, that being the Ann Arbor route. While this is true, Conrail and other large railroads have taken other separate and not directly related actions which are intended to limit the availability and use of the Ann Arbor route to and from the East. The result is that both of GB&W's Eastern connections are in jeopardy.

Conrail is determined to force as much traffic as possible to and from the West through the Chicago terminal. Some of its efforts in that regard are also resulting in eliminating traffic that the GB&W would otherwise participate in via its interchange with the Ann Arbor. A specific example was Conrail's refusal in recent months to concur with GB&W in a proposed competitive joint rate on plastics over the Ann Arbor route.[4] In that action Conrail held down its joint rate via Chicago to take advantage of only 3 percent of a 5 percent general freight rate increase

[1] The Conference Committee deemed it "extraordinary," Report of the Committee on Conference on S.1946, H.R. Report No. 96-1430, September 29, 1980, p. 112.

[2] See S. 796, section 104, 96th Congress, 1st Session.

[3] Changes in Routing Provisions—Conrail—July, 1981, ICC Docket No. 38676.

[4] See Appendix A; copy of GB&W proposal dated May 6, 1981, and Conrail's refusal to concur dated June 5, 1981.

authorized by the ICC in Ex Parte No. 386 while refusing GB&W's proposal for an identical 3 percent hold down for the same traffic via the GB&W—Ann Arbor route. So, while Conrail justifies the closing of the GB&W's Eastern connection via Chessie on grounds the Ann Arbor is still available, it is whittling away at the viability of the Ann Arbor route by such practices as the described refusal to concur with GB&W in an equally competitive rate hold down on plastics when moved via Ann Arbor instead of via Chicago.

Actions of other large carriers further compound the problem for the GB&W. For example, the Union Pacific has filed a tariff proposing to cancel joint rates on soda ash via the Ann Arbor route. The ICC Suspension Board initially refused to suspend the Union Pacific Tariff; but on Reconsideration, the Commission's Division One has suspended the tariff and ordered it investigated.[5] While I do not intend to litigate the merits of the case before this Committee, and I'm confident the Interstate Commerce Commission will properly conclude the proposed route cancellation is not in the public interest, it clearly is a predatory pricing practice involving undue concentration of market power and is unlawful discrimination. The entire thrust of the proposed rate/route cancellation is the principle advanced by the Union Pacific that it has the arbitrary right to determine what is in the public interest—not the ICC.

All examples cited are designed to reduce competition by eliminating GB&W bridge traffic, further shifting economic power to those currently possessing no small measure thereof.

Burlington Northern Petition to Reopen Finance Docket No. 21478 under the auspices of the Staggers Act poses an even more threatening position. The BN proposes the elimination of the so-called "DT&I traffic protective conditions" which were imposed as a condition of approval of its 1970 merger. In order to secure the alleged advantages of that merger, Burlington Northern had voluntarily agreed to the imposition of the conditions. Now, contending that the Staggers Act has changed things, Burlington Northern seeks to be relieved of its agreement to observe those conditions. It is obvious that if those conditions are removed, certain traffic that now moves via GB&W to and from Eastern and Southern destinations will no longer do so. We are so dependent on this major Class I carrier for joint rates/routes and service because fully fifty (50) percent of carloads handled on the GB&W system move from, to, or via BN RR. In 1980 GB&W system carloads totaled 63,245 and 31,655 of those were interchanged with BN RR. Should the I.C.C. authorize removal of DT&I conditions, it would be devastating to the GB&W. We think it is vital that both the Congress and the Commission review the cumulative effect of these, perhaps unconnected actions, in its implementation of the Staggers Act and this assessment of it impact.

Big is not necessarily good. In fact, there is no real evidence to indicate that mammoth organizations, such as Conrail and Burlington Northern, can perform more efficiently or make a greater contribution to the public interest than smaller ones. Yet the Staggers Rail Act is being systematically used by some of the large railroads to capture traffic away from the smaller roads and eliminate us as competitors.

The Staggers Rail Act placed heavy emphasis upon the role of competition in the market place (see the National Transportation Policy in 49 U.S.C. Section 10101 and 10101a). Despite these admonitions to promote competition, the joint rate and route closing actions of Conrail, coupled with the proposals of GB&W's Western carriers (BN and UP), seriously threaten to eliminate a competitive route between the Northwest and the South and East.

We are aware of nothing in the Staggers Act directing or suggesting that traffic protective conditions, imposed after extensive hearings to preserve small lines competitive routes against monopoly power, should be withdrawn. But that is precisely what is being sought in the BN petition.

We are likewise not aware of anything in the Staggers Act directing or suggesting that a large profitable railroad like Union Pacific should be authorized to cancel a joint rate over our small railroad when UP's revenue to variable cost ratio on such traffic ranges from 180 to over 300 percent. But that is precisely what is being sought by the Union Pacific's proposed cancellation of soda ash joint rates.

Furthermore, we are not aware of anything in the Staggers Act or elsewhere directing or suggesting that a large railroad like Conrail should be authorized to cancel all our joint rates to, from, or over Conrail's lines when a certain intermediate railroad is included in the joint rate. Such action is not a cancellation of a joint

[5] Suspension Case No. 70565.

rate as authorized by the Staggers Act but the cancellation of competitors by cancelling all their joint rates via a particular connection.

Under the prevailing construction of section 217 of the Staggers Act, Conrail does not even have to identify the specific joint rates over which it may not have a satisfactory revenue to variable cost ratio. It simply files a tariff cancelling all of them via particular routes, and the victims are faced with the impossible task of developing Conrail's revenues and variable costs for each rate. We think the provision of the Staggers Act that countenances such heavy handed actions should be repealed or significantly amended.

This brings me to another way in which the new statute is not working as it should. Because of the danger to small railroads from threatened surcharges and rate cancellations, Congressman Lee of New York was successful in obtaining a small measure of assistance in Staggers which calls for the Commission, when requested, to determine the revenue to variable cost ratios.[6] However, rather than provide smaller railroads with protection against the massive power of their major connections as envisioned by the Lee amendment, the Commission's proposed rules for its implementation substantially erode the effect of the Lee amendment.[7]

Without any justification of which we are aware, the Commission's proposed rules for assisting small railroads in developing revenue to variable cost data calls for data to be prepared using a formula that is unfair to the railroad seeking to protect itself. Under the statute if a railroad whose rate is being cancelled or surcharged needs help in developing the revenue to variable cost ratio over the cancelling of surcharging carrier's lines, it may provide certain information to the Commission which will in turn make the necessary computations. However, by requiring the use of minimum weights only, the Commission guarantees that a finding favorable to the railroad whose rate is being cancelled or surcharged will be more difficult. It does this by requiring the submission of minimum weights which are multiplied by the tariff unit rates to determine the shipment's revenues, which are then compared with its variable costs. Since the vast majority of shipments are loaded to weights which substantially exceed the minimum, the revenues computed in this fashion are always lower than actual revenues. Unlike a determination of variable cost, which is difficult, a determination of actual revenues is a simple matter, and there is no need whatever to utilize a formula computation which estimates revenues.

In an attempt to justify the Commission's use of something other than actual revenues, Conrail cites the statute and its legislative history explaining why a formula is necessary to determine variable cost. There is no dispute about the need for a formula in determining variable costs. It is virtually impossible to assign costs accurately and precisely among various services and certainly no way to know with certainty what specific actual costs are incurred for a specific service. This problem does not exist with revenues. The actual revenue for particular traffic can be and should be used.

It is bad enough that the Commission is using estimated revenues where it is called upon to make the revenue/cost calculations but it is beyond justification for the Commission not to use actual revenues where one of the parties produces them. If nothing else, this oversight hearing should result in providing the Commission some clear instructions to use actual revenues in determining the revenue/cost ratios. Otherwise, carriers like ours whose joint rates are being cancelled and surcharged by our large connections, are being unfairly prevented from utilizing the full protection the statute provides.

As a consequence of the Staggers Act, small railroads are having increasing difficulty in developing competitive joint rates with their large connections. Some of these connections apparently view the Act as making it no longer necessary for them to enter into joint rates with the small carrier, particularly where that joint rate would compete with a single line or other joint rate in which the small carrier does not participate and as to which the large carrier receives a greater portion of the revenue. We know of nothing in the Staggers Act or elsewhere that eliminates the requirement upon railroads to participate in joint rates providing a through route service with their connections.

Coupled with these blantant attempts to remove the competitive viability of the weaker Class I carriers and smaller Class II (GB&W) and Class III's through what I term predatory and discriminatory practices, we daily are faced with the necessity of securing connecting lines' concurrence to permit GB&W routing on all new rates/routes. Those carriers with massive economic power by reason of financial capability, equipment, number of solicitors, and productive territories which are often

[6] 49 U.S.C. 10705a(h).
[7] I.C.C. Ex Parte No. 389.

locally served by one rail carrier are delaying and many times refusing to permit normal routes, thereby holding movement to their longest possible haul, completely excluding GB&W. This ever debilitating action to strengthen concentrations of market power is an insidious encroachment of the principles and goals of the Staggers Act and our free enterprise system.

In summation of the routing situation, when GB&W route is in the tariff it guarantees us nothing but the right to compete. Traffic does not flow to us other than at our shipper's option. When that customer no longer has the right to route freight over our line, it is clearly discriminatory to both the customer and GB&W. As small as the GB&W is, we enjoy being in the competitive transportation field, but we can provide no alternative—no effective competition—with our hands tied. Ninety-eight percent of our traffic is interchanged with other carriers, and we could not survive on our two percent local business.

A final area of concern to GB&W has to do with Section 213 of the Staggers Rail Act (49 U.S.C. 10505) pursuant to which exemptions from regulation are granted by the Commission. Obviously, in an industry in which individual members are so interdependent, small entities are less capable of surviving in an exempt environment. Conrail's proposal that all traffic moving in boxcars to, from, or via the lines of Conrail shall be exempt from regulation is most onerous.[8] The proposed exemption also would remove all regulation over the boxcar hire rates and the Commission's authority over the use and distribution of boxcars.

GB&W has a substantial amount of originating traffic on its lines and has acquired high quality equipment to serve that need. The last thing we want to see happen is for Conrail to be able to exercise its considerable economic and market power in controlling the use and setting the rates for the use of our quality equipment.

Under Conrail's proposal to exempt boxcar traffic, GB&W would have little, if any, ability to regain use and control of our equipment when needed or to ensure adequate compensation for its use. We do not think Congress envisioned such a wholesale exemption of traffic depending upon what type of freight car it moves in. Much of the boxcar traffic involves movement to, from, or via Conrail and its service performance is very poor. If that exemption is granted by the Commission, there will be no incentive for us to acquire new boxcars and every reason to worry about having an adequate supply of quality equipment to meet our customers' requirements.

Congress has often expressed concern about boxcar supply and should be vitally concerned about this proposed exemption. Today the major problem in boxcar supply is the current surplus of boxcars caused by business conditions. However, periodically for nearly 100 years, Congress and the Commission have joined with railroads in coping with sometimes very severe shortages. When business returns to a level that again brings car shortages (as it always has in the past) we cannot afford to have our equipment controlled by the party having the greater economic power but giving the least efficient service. Nor do we believe the shipping public and the interests of national defense can afford it.

We urge the Committee's perusal of the foregoing and stand ready to further assist wherever possible.

[Telegram]

EXHIBIT A

Mr. J. A. HAGEN,
Senior VP—M&S CR,
Philadelphia, Pa.

Refer item 640 series, X386 plastic materials and exception 2 covering movements via CR. Movement to Green Bay, Wisc. consignee on GBW. Please advise if you concur in addition of following in exception 2, item 640—to GBW station, Green Bay, Wisc. via CR Toledo, Ohio AA or CO Kewaunee, Wisc. GBW.

V. J. MALONEY.

[8] I.C.C. Ex Parte No. 346 Sub No. 8; Petition To Exempt Conrail Boxcar Traffic From Regulation.

Mr. J. M. SOUBY,
Chairman, Executive Committee,
Western Railroad Traffic Association, Chicago, Ill.

Mr. V. J. MALONEY,
Greenbay & Western Railroad,
Green Bay, Wisc.

Mr. K. P. PIERSON,
Ann Arbor Railroad System,
Owosso, Mich.

This refers to your June 2, 1981 wire regarding exception 2, ex parte 386 covering plastic materials (STCC 28211).

Conrail withdraws its concurrence with the application of the 2-percent increase on traffic between points on the GBW and points on CR when routed via CR-Toledo, Ohio-AA-Kewanee, Wisc.-GBW and the reverse. This is not a longhaul route and the 5-percent increase will apply.

D. L. BODNAR,
Manager—Pricing, Conrail.

Senator DANFORTH. Gentlemen, thank you very much.

The next panel is the utility panel. Robert Lundgren, J. Raymond Clark, and C. Michael Loftus.

STATEMENTS OF ROBERT LUNDGREN, EXECUTIVE VICE PRESIDENT, DETROIT EDISON CO.; J. RAYMOND CLARK, ESQ., REPRESENTING LOUISIANA UTILITIES AND EDISON ELECTRIC INSTITUTE; AND C. MICHAEL LOFTUS, ESQ., REPRESENTING WESTERN COAL TRAFFIC LEAGUE, AMERICAN PUBLIC POWER ASSOCIATION, NATIONAL RURAL ELECTRIC COOPERATIVE ASSOCIATION, AND CONSUMER OWNED POWER COALITION

Mr. LUNDGREN. Thank you, Mr. Chairman.

I represent Detroit Edison and the Edison Electric Institute. I have on my right here Mr. Clark, who represents Louisiana Utilities, and also EEI; on my left, Mr. Mike Loftus, who represents the Western Coal Traffic League, the American Public Power Association, the National Rural Electric Cooperatives, and the Consumer Owned Power Coalition. We appreciate the opportunity to appear before your committee today.

The electric utilities are concerned about the ICC stewardship of the Staggers Rail Act, because they must depend upon the railroads for transporting their enormous coal requirements. Rail-transported utility coal paid $3½ billion, or about 70 percent of the railroads' reported 1980 revenues from all coal. Since the rate ceiling for utility coal is about 160 percent of variable costs, coal's 1980 contribution above variable cost was $1.3 billion. That's about the same as the railroads' total 1980 net railway operating income from all traffic. The Nation's 10 most prosperous railroads transported 80 percent of U.S. coal.

Three of these, the N. & W., Missouri Pacific, and the Southern—have just reported all-time record third-quarter earnings of a very healthy $359 million in working capital. The N. & W.'s prime concern is reported by the Wall Street Journal as focused on the acquisition of tax shelters. These strong earnings reports are not necessarily typical, but they call into question the recently adopted standard of revenue adequacy. According to the ICC, all three of these apparently prosperous railroads are classified as revenue-

inadequate. We think there is something wrong with any standard which says that the N. & W. is in financial trouble.

Shippers also think the Commission erred in its decision on ex parte 320 to change its definition of market dominance so as to make it more difficult for us to prove we are captive shippers and entitled to rate relief.

We are also concerned with the decision to let the railroads impose orderly rate increases beyond the actual rise in their costs, and with its proposal being considered in ex parte 347 to raise the permissible rate ceilings on coal. We are gravely concerned that these rulings will be taken as an invitation to the U.S. railroads to raise their rates on captive traffic to new highs. Several are already rushing to the open door.

In June of this year, Detroit Edison and other utilities served by the Burlington Northern were all told that the Burlington Northern intended to use the "freedoms of the Staggers Act" to raise our coal rates. In August, the Burlington Northern asked the ICC for permission to raise Detroit Edison's western coal rates from $9.45 to $17.07 a ton—an 87-percent increase. If Burlington Northern gets this permission and makes good its threats, the result would cost Michigan ratepayers about $30 million a year. In 5 years, when the Burlington Northern will more than double its rates, it will cost $66 million a year.

We do not think Congress expected or intended the Commission to open the door for extravagant rate increases unrelated to increases in railroad operating costs. We think it is timely and necessary for Congress to admonish the Commission about such rulings, and remind it that the goal of railroad revenue adequacy cannot be pursued at the expense of other vital policy goals stated in the Staggers Act.

At a time when the railroads are becoming preoccupied with tax shelters to preserve their record earnings, the Commission should at least give equal time to that policy goal which permits it to seek reasonable rates for captive traffic.

[The statement follows:]

Statement of Robert W. Lundgren on Behalf of Detroit Edison Co., and Edison Electric Institute

My name is Robert W. Lundgren and I am Executive Vice President-Operations of the Detroit Edison Company (DE). I am also Chairman of the Coal Rate Regulatory Task Force of the Edison Electric Institute (EEI). EEI is an association of investor-owned electric utility companies. I am submitting this testimony on behalf of the members of EEI as well as my own company. I appreciate the opportunity to provide this Subcommittee with our views concerning the ICC's implementation of the Staggers Rail Act of 1980.

Needless to say, I shall focus upon freight rates. As you know, the likely effect of the proposed Rail Act on coal rates was substantially debated in Congress when the legislation was under consideration. This is because of the enormous quantities of coal that must be shipped for electric utility use and because most utility coal movements are entirely captive to the railroads.

As a consequence of conversation to coal, construction of a new coal-fired generating units and longer hauls, not to mention escalating rates, railroad revenues from coal transportation have increased dramatically in recent years and are expected to further increase during the next decade. The reported revenue in 1980 for all railroad traffic in that year was $4.925 billion. Of this, utility steam coal represented at least 70 percent or $3.5 billion. We further estimate, conservatively, that the $3.5 billion utility freight bill for 1980 includes a contribution above the associated variable costs of service of approximately $1.3 billion. As it happens, this is roughly

equivalent to the total Net Railway Operating Income (NROI) for the railroads in that year.

It might be interesting to note that the ten railroads classified by the ICC as being of the highest investment grade accounted for 81 percent of the 1980 coal revenues. Hence, we see a close correlation between coal traffic and railroad profitability. Further confirming this correlation are the recently reported record earnings for the third quarter 1981 by Norfolk & Western, Missouri Pacific and Southern reflective of increased coal traffic on those lines. It's interesting to note that the same issue of the Wall Street Journal that reported N&W's record earnings also reported an effort by N&W to minimize its income tax liability by acquiring deficit companies. The fact that the ICC has now classed carriers like N&W, Missouri Pacific and Southern as revenue inadequate demonstrates the abysmal lack of plain common sense manifest in the ICC's revised revenue adequacy determination.

Coal transportation charges translate through fuel adjustment clauses into the consumer's electric bill and, hence, are a substantial ingredient in the inflationary spiral. Thus, there is a substantial national interest—reflected clearly in the Rail Act and its legislative history—that coal rates not be allowed to rise above a reasonable level. It is too early to assess definitively the impact of the ICC's implementation of the Rail Act, for several reasons. First of all, several of the ICC's decisions have been challenged in court and the results of these appeals will not be known for some time. Also, the ICC consideration of the rulemaking for setting maximum rate guidelines for shipments is still pending.

However, there are several of the Commission's decisions under the Rail Act that are cause for grave concern to us. We think these decisions open the door to abuse of the Rail Act's provisions by the railroad. These decisions relate to the procedures for determining increases in railroad rates to cover inflationary costs increases; the procedures for deciding whether railroads have market dominance over a movement, that is, whether the ICC has jurisdiction to consider a shipper's complaint; and the Commission's new standards for determining whether a railroad is earning adequate revenues.

Other speakers will address these Commission's rulings in more detail. EEI's concern, however, may be summarized as follows:

The Commission has adopted the AAR Price Index as the "cost adjustment factor" increasing railroads rates to account for inflation without making adjustments for productivity gains and other factors that influence the output unit costs of rail service.

The Commission has scrapped the previous regulations which shippers could rely on in proving that a railroad has market dominance and has determined that product and geographic competition can be considered in denying carrier market dominance.

The Commission has discarded its previous standards for determining whether railroads are earning adequate revenues and has substituted new guidelines, without justification, that seem to show that no large railroads, even apparently prosperous lines like the Southern, N&W and UP, are "revenue adequate".

Although the Commission has not yet decided the proceeding to set guidelines for determining maximum rail rates, we are gravely concerned with its proposed guidelines. Under the guise of reallocating fixed railroad costs, those guidelines would arbitrarily and deliberately assign a heavy burden on the rates for coal and other heavy volume bulk traffic.

We are fearful that the railroads will interpret these recent rulings as an invitation for further increases in the already high coal rate structure. Indeed, the coal carrying lines are already pounding on the rate increase door. They have, of course, taken full advantage of the Commission's over-generous cost-pass-through increases—which have run half-again higher than the PPI index for the economy as a whole. But these inflation-related increases are likely to be only the beginning. The SCL has imposed a surcharge, over and above the quarterly cost-related increases, and Florida Power reports that its rates have, accordingly, risen by 17-½ percent, in the year since the Rail Act's passage. The C&O Railroad has published special increases in its river coal rates as high as 40 percent, and the ICC declined to investigate. Of still greater importance to DE, the Burlington Northern Railroad (BN) has put all of its utility coal customers on notice by a June 15, 1981 letter that it "will resort to the Freedoms of the Staggers Act" as necessary to "change significantly" its coal rates. DE is now contesting BN's requested permission from the ICC to increase our freight bill for western coal by about $30 million annually.

To summarize our views, the Rail Act reflected a compromise of sharply divergent viewpoints that, properly implemented by the ICC, could reasonably satisfy the sometimes conflicting policy goals of Congress. For the reasons I have stated, the ICC's interpretation of that statute has reflected a preoccupation with some goals,

ike railroad revenue adequacy, and an indifference to others, like reasonable rates for captive coal.

[The following information was subsequently received for the record:]

QUESTIONS OF SENATOR RIEGLE AND THE ANSWERS THERETO

Questions. Since you "pass-through" most of any increases in your delivered fuel cost, why do you protest rail increases so vehemently?

Answer. Our right to continue "passing through" these increases is a privilege we must earn. We cannot, therefore, watch the railroads heap further non-cost-related increases on coal, without protesting on behalf of our ratepayers. While we bear a part of any increase, without immediate reimbursement, it is our ratepayers who bear the brunt of all increases in the delivered cost of fuel. We must act as their trustee in this regard and take this responsibility seriously.

Question. How can you object where railroads merely exercise their "freedoms under the Staggers' Act" as you say the BN told you it intended to do?

Answer. The BN sees those freedoms as including the rights: (1) to violate our contract which set the rail rate; (2) to make quarterly "catch-up" increases beyond the experienced impact of inflation on their coast; and (3) to charge what they call "Ramsey Prices," which are really a form of profit-maximizing monopoly rentals.

I am not really concerned about their intentions—which will always include higher prices for their captive shippers. I am concerned about the ICC's recent rulings which (except for its firm stance on contracts) may have opened the door to the implementation of such a callous policy which is not only detrimental to ourselves but also to our customers.

Question. Why should the ICC or Congress concern itself with the freight bills paid by electric utilities when it is the railroads who are experiencing financial difficulties?

Answer. We believe it is bad public policy to allow railroads to exploit monopoly power, even where they may need the excessive profits they can thereby extract from their captive customers. Moreover, coal rate increases primarily benefit those wealthy railroads who carry over 80 percent of the coal. BN and CSX, who transport most of Detroit Edison's coal, have higher credit ratings than Detroit Edison does. Standard & Poor rates Detroit edison Bonds "BBB-" where BN has a "AA" and CSX an "A" rating.

Senator DANFORTH. Thank you very much, Mr. Lundgren.

Mr. Clark?

Mr. CLARK. Thank you very much, Mr. Chairman. We have heard much this morning about coal and differential pricing. I think it must be perfectly obvious from what we have heard that it is the electric ratepayer who is to have the privilege, through the coal rates, of paying differentially priced rates and subsidizing what the railroads conceive to be adequate revenues.

This was a subject of considerable discussion in the debates prior to the enactment of the Staggers Act, and there was a real effort made to reconcile the legitimate interests of the railroads in achieving greater rate freedom, while at the same time preserving regulations where there is no effective competition—as in the case of captive coal.

Regrettably, however, the Interstate Commerce Commission has not seen fit to preserve this balance. As they say in the movies: Any resemblance between the act and the Commission's interpretation of the act "is entirely coincidental."

We cannot acquiesce in Chairman Taylor's glowing appraisal of what the Commission has accomplished. I think it must be evident from Mr. Dempsey's general endorsement of what the act has accomplished that the utility coal shippers aren't doing very well. Differential pricing is a concept that we can accept. It contemplates, however, that there be self-help efforts made by the rail-

roads, to minimize losses due to inefficiency, before you start spreading differential pricing over captive traffic. Indeed, the Staggers Act jurisdictional threshold, 160 to—now 165 percent—has some differential pricing included.

We have heard nothing from the Interstate Commerce Commission about the conditions precedent to differential pricing that are provided in the Long/Cannon amendment to the Staggers Act, to wit: elimination of noncompensatory traffic; maximize the contribution from your marginal traffic; equitably distribute your revenue shortfall, if any, after you have done that, over all captive traffic. The Commission is called upon to make these determinations, to consider these factors. It is impossible for them to consider these factors because they have taken no steps to develop the data, as to, for example, noncompensatory traffic, which obviously is in the possession of the railroads.

Differential pricing, of course, ties into revenue adequacy, and revenue adequacy was indeed a 4-R Act concept that has been further implemented in the Staggers Act. We find the zone of rate flexibility increases—the 6 percent and the 4 percent—tied to determination of revenue adequacy. Indeed, the 4 percent is to be withheld from revenue-adequate railroads.

Now, at the time the act was enacted, there were 13 class 1 railroads classed as revenue-adequate. Those railroads, like the Union Pacific and the Norfolk & Western, and the Southern, haven't gotten any poorer in the intervening time. Quite the contrary, their earnings have improved. Why are they now classed as revenue-inadequate? Because the Commission has simply jettisoned the yardstick for determining revenue adequacy and has come up with a new yardstick which just defies human credulity.

There is no way that you can class the N. & W. seeking offsetting tax credits as a revenue-inadequate railroad, but that's where the Commission formula would take you.

So we have real concerns, Mr. Chairman, that the balance that was so laboriously achieved, which undertook to preserve a forum for captive shippers, notably coal shippers, has been upset by the rulings by the Interstate Commerce Commission in the various rulemaking proceedings.

Thank you.

[The statement follows:]

STATEMENT OF J. RAYMOND CLARK ON BEHALF OF LOUISIANA UTILITIES AND EDISON ELECTRIC INSTITUTE

I appreciate and, indeed, welcome this opportunity to meet with this Subcommittee to review the first year of experience under the Staggers Rail Act of 1980 from the standpoint of the shippers and shipper organizations enumerated in the accompanying Appendix to this testimony.

To briefly identify myself, I have practiced actively before the Interstate Commerce Commission since 1954, most recently representing shippers in rail rate matters. I had the privilege of participating with members of the Committee's staff as well as rail and shipper representatives in many of the discussions that preceded enactment of the Staggers Act and can attest from personal experience to the sincere effort made by the staff—and the members of Congress—to reconcile these divergent interests. I think the bill that finally emanated did a reasonably commendable job of striking a fair balance among the interests of the rail carriers, shippers and the general public. Naturally, there are certain provisions of the Act as to which shippers—and my remarks refer to captive shippers—are less enamored but I am certain that some of our railroad brethren have exactly the same view.

Candidly stated, therefore, it was the shippers' position at the time, and continues to be their position, that they can live with the Staggers Act if the legislative intent of that Act is fairly implemented by the Interstate Commerce Commission. That has not occurred, unfortunately. Rather, the I.C.C., in a series of rulemaking proceedings and also in specific complaint cases, to which I shall later refer in some detail, has drastically misinterpreted significant provisions of the Act to the detriment of the shipping public and has pending before it other proceedings which may further subvert the legislative purpose. On the other hand, there are significant aspects of the Staggers Act, notably including the provisions of the Long-Cannon amendment, that have not as yet been addressed by the I.C.C.

Following is a brief discussion of the actions taken by the Commission in purported implementation of the Act:

1. In Section 203(a) (specifically as now codified in 49 U.S.C. 10707a(a)(1)(B)), the Act provides for the determination by the Commission of a quarterly "rail cost adjustment factor" which may be applied to all rates without challenge. The Commission has undertaken to promulgate such a factor in Ex Parte No. 290 (Sub-No. 2), Rail Cost Recovery Procedures; decided April 8, 1981, now pending on Court review upon peitition of numerous shippers. What the Commission adopted as the cost factor was the very AAR price index that was first proposed in the Senate bill, vigorously objected to by shippers, and thereafter deleted. There was substantial testimony at the time stressing the impropriety of using a price index to measure changes in cost—the major deficiency, simply stated, being lack of consideration of improved productivity, some of which is made possible by shipper investment and cooperation. The Commission candidly recognized in its decision in Ex Parte No. 290 (Sub-No. 2) that the AAR index overstates increases in cost but nonetheless decided as a "policy" matter to permit increases in rates to be measured by that Index.

Let me hasten to emphasize that the shippers whom I represent acknowledge the right of the railroads, like any other business, to respond to inflation in their rates and to recover increased costs. We object most strenuously, however, to rate increases under the pretext of a dollar for dollar offset to inflation that are expressly designed to improve profits in addition to compensating for increased operating costs. Other provisions of the Act afford the railroads an opportunity to improve their profits but that is not the purpose of the cost adjustment factor. We believe that the Congressional intent has been misinterpreted by the Commission in this regard.

2. Section 205 of the Staggers Act and specifically new Section 49 U.S.C. 10704(a)(2) made some minimal changes in the provisions concerning railroad revenue adequacy first enacted in the 4-R Act. In essence, the Staggers Act permitted revision of preexisting revenue adequacy standards "as necessary" and directed the I.C.C. to get on with the task of annual revenue adequacy determinations, only one of which had been made previously. In its decision of March 30, 1981 in Ex Parte No. 393, Standards for Railroad Revenue Adequacy, the Commission seized upon these minor changes in the law to jettison their earlier standards in favor of a new approach under which virtually no Class I railroad, however profitable, is found to be revenue adequate. As the Subcommittee is aware, the term "revenue adequacy", first articulated in the 4-R Act, appears in many contexts throughout the Staggers Act. It is our view that the Congress believed that it was dealing with a known and quantified factor when it used this term which already had a definitive meaning.

The Commission has taken a contrary position, the ramifications of which are substantial and widespread. To cite one illustration, the Staggers Act provides that zone of rate flexibility increases after 1984 be withheld from revenue adequate railroads and that similar increases prior to 1984 be scrutinized in the light of revenue adequacy determinations. At the time the Act was pased, the Commission, in the only revenue adequacy determination made, had found 13 of the 36 study Class I railroads to be revenue adequate.[1] It now tells us, based on the most recent determination using different standards, that there are only three revenue adequate railroads, specifically Clinchfield, Pittsburgh & Lake Erie, and Ft. Worth & Denver (the latter a Burlington Northern subsidiary). Superior earning lines like N&W, Southern, UP, MoPac, DRGW and C&O, earlier found to be revenue adequate, are now classed as needy, not because of changed circumstances but by use of a different "yardstick". In all fairness, I should add that Chairman Taylor in his concurring expression in that proceeding (Ex Parte No. 416) indicated that he did not accept the revised formula.

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[1] Ex Parte No. 353, Adequacy of Railroad Revenue (1978 Determination), 362 I.C.C. 199, January 31, 1980.

3. Section 202 of the Staggers Act grafted a significant additional jurisdictional hurdle for captive shippers upon the market dominance condition precedent imposed by the 4-R Act, specifically the annually increasing rate-to-variable cost ratios. But apart from these ratios, market dominance, like revenue adequacy, was a known factor when the Staggers Act was considered. Pursuant to 4-R Act requirements, the Commission had promulgated market dominance rules that had both withstood judicial scrutiny and been applied in numerous cases.

Apart once again from the added jurisdictional ratios which supplanted the earlier I.C.C. rate-cost presumption, we can perceive no Congressional purpose to change the market dominance concept as it then existed. Product and geographic competition were expressly authorized by Section 205 to be considered as possible factors bearing upon rate reasonableness but that section just as expressly made it clear that "proper scope of the term 'market dominance'" was unchanged.

The Commission, however, has once again drastically changed the market dominance ground rules, perceiving a legislative purpose to do so where none in fact is found in the Act, and proposals to this effect had been rejected.[2] Notwithstanding, the Commission on July 8, 1981 vacated its earlier rules in favor of "guidelines" and, in an admitted reversal of its original interpretation of the same unchanged 4-R Act statutory language, decided to consider product and geographic competition as proving effective competition, i.e. lack of market dominance.[3] The net effect is to hold that a shipper now moving 100 percent of its traffic, say coal, from Mine A to Generating Station B over the only rail line linking those points, may nevertheless be denied access to the Commission for rate relief if the latter concludes that it could just as well buy its coal from Mine C on another railroad or convert its boilers to burn another fuel. Of course, if the shipper pursues this "competitive" suggestion, it would likewise be told that it is not captive to the second railroad because it could switch back to Mine A, necessarily blithely ignoring contractual committments in both cases.

Again we do not believe that the Congress in enacting the Staggers Act intended or even authorized the complete "flip flop" in the established market dominance test that the Commission has since effected, based upon its interpretation of that Act.[4]

4. Section 214 changed significantly the balance between the I.C.C. and the State Commissions, narrowing State independence by making them obtain certification from the I.C.C. of their intent to follow Federal standards and procedures. The statute also gave the I.C.C. exclusive jurisdiction over general rate increases, inflation adjustment increases, and fuel surcharges.

The Commission, however, has taken these changes a good deal farther than the law provided. In a recent case now being litigated in the 7th Circuit, the I.C.C. approved a completely intrastate increase specifically on coal by the simple expedient calling it a "general rate increase"—although the Commission defines "general" increases in its rules as those on "a substantial number of commodities." An increase only on coal cannot be any stretch qualify in that category.

I.C.C.'s action, furthermore, was not as to some future increase. It was to improve increases which the State of Indiana had previously held down in 1979 and 1980. Thus, it purported to undo actions—and without any hearing at that—which had been taken before the Staggers Act.

I have tried to describe briefly the major areas in which the Commission has taken final action, in misplaced reliance upon the Staggers Act, that subverts the Congressional purpose in both the 4-R Act and Staggers Act of providing to captive shippers a forum, admittedly drastically curtailed by the 180-day challenge period of the latter statute, in which their rate reasonableness complaints can be considered. Now let me briefly allude to some matters still pending, of similar concern.

The railroads, doubtless emboldened by their success in persuading the Commission to use the AAR price index for automatic rate escalation purposes, have recently petitioned the Commission to substitute this same index for established methodology in updating costs for use in determining the jurisdictional threshold. The acknowledged purpose is to make pending complaints attacking existing rates subject to dismissal by in effect first applying the current Staggers Act level of 165 percent—instead of the 160-percent level in effect when the complaints were filed—

[2] Former Congressman Robert C. Eckhardt has written a very enlightening article on this subject in the September 1981 issue of the I.C.C. Practitioner's Journal.

[3] Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations and Consideration of Product Competition, 365 I.C.C. 118.

[4] Once more in fairness to Chairman Taylor, he has himself raised questions regarding both the legality and practical effort of this ruling. See Taylor concurrence in decision served October 28, 1981, in Ex Parte No. 320 and Ex Parte No. 320 (Sub-No. 2).

and then changing the current Staggers Act level from 165 percent to 184 percent through the simple expedient of increasing the cost element in the comparison. This ignores the fact that the present levels were fixed by Congress in light of current costing methodologies. This proposal is very much like one football team proposing that the distance from midfield to its goalline be increased from 50 to 75 yards.

Also pending, indeed long pending, and admittedly not claimed as specifically sanctioned by the Staggers Act, is Ex Parte No. 347, Coal Rate Guidelines—Nationwide, in which the most serious of a number of Commission proposals is to change the method of computing full costs by increasing the allocation of constant costs on this major captive commodity for the precise reason that it is captive traffic. This proposed change means that any shipper who first succeeds in running the jurisdictional gauntlet now erected by the Commission will be met thereafter with substantially higher rates than under the earlier test based upon revised, and, of course, increased "costs." The underlying theory of this proposed Commission revision is termed "demand elasticity." More simply stated, however, it amounts to saying that the greater the railroad's monopoly power over a rate, the higher the rate may be. We consider this to be precisely the opposite of the Congressional purpose in both the 4-R and Staggers Acts to protect captive shippers against monopoly abuse.

The Staggers Act codifies the right of railroads and shippers to enter into long-term transportation contracts and I'm sure this Subcommittee is interested in the extent to which captive shippers have been able to use that provision. The answer in a nutshell is not at all. Contracts can be negotiated only between parties with near equal bargaining power. Captive shippers have none—unless there is preserved the option of seeking and obtaining rate relief through regulation. The more the Commission erodes the shipper's access to this forum through circumscribed jurisdictional tests as earlier described, the less the bargaining "clout" of that shipper. There can be no possible inducement to a railroad to offer a reasonable contractual rate if it is free to charge any rate it wishes. The best way to stimulate long-term contracts is to bring the railroads to the bargaining table because they prefer compromise to litigation. If a shipper can't litigate, why should the railroads show any restraint in pricing?

Another source of real concern arising under the Staggers Act is the procedure to be employed by the Commission to handle the approximately 800 complaints filed under Section 229. The cut-off date for challenging existing rates was March 30, 1981. To my knowledge not one of those complaints has reached the evidentiary stage. The Commission shows recent signs of coming to life and late last month held a conference to discuss procedure. The conference resulted in some imaginative handling the "one shot" work load. I believe, nonetheless, that it would be helpful if the Congress made it clear that while the Staggers Act fixed a cut-off date for attacks upon existing rates, it did not intend Section 229 complaints to receive any less procedural safeguards or substantive consideration than any other complaint.

As I stared earlier, the Commission has left certain aspects of the Act untouched while inconsistently finding legislative intent in other areas that cannot be reconciled with the Act and its legislative history. The Long-Cannon provisions are of primary significance in this context. Section 203 of the Staggers Act (now 49 U.S.C. 19707a) and specifically subparagraphs (3)(2) (B) and (C), requires that the Commission consider railroad efforts to eliminate noncompensatory traffic, maximize contribution of marginal traffic and evaluate the mix of traffic in determining the reasonableness of proposed increased rates or existing rates challenged by complaint. No guidelines have been established to carry out these provisions. No effort has even been made to develop the data to quantity these mandatory considerations, all of which obviously the railroads must be required to produce. In other words, the Commission is no closer today than it was before to a determination of how much of a particular carrier's claimed revenue shortfall is attributable to pricing errors on other traffic. Captive shippers are still called upon to subsidize revenues without any demonstration that the carrier has itself done its best to improve revenues.[5]

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[5] Lest one be tempted to assume that I exaggerate the volume of below-cost traffic, following are two glimpses into the hidden abyss of railroad pricing policies:

(1) The Initial Decision of March 3, 1981 in No. 36114 (Sub-No. 1), *Potomac Electric Power Company* v. *Consolidated Rail Corporation*, finds that: "Conrail experienced an increase in deficit below variable costs from noncompensatory traffic of from approximately $117 million in 1977 to $277 million in 1978". (p. 14)

(2) By letter of September 2, 1980 to the Chairman of the Subcommittee on Oversight and Investigations of the House Committee on Interstate and Foreign Commerce, then-Chairman Gaskins of the I.C.C. stated that in 1977 below variable cost traffic showed revenues of $2.3 billion and costs of $3.1 billion, i.e. a net deficit of $800 million. I.C.C. Ratemaking Noncompetitive Markets—Oversight, August 28, 1980, Serial No. 96-176, p. 84.

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While it is not generally the purpose of this testimony to suggest modifications of the Staggers Act, the Subcommittee should be aware that the term "unadjusted Rail Form A costs" for the "particular transportation" as employed in Section 202 (49 U.S.C. 10709(d)(3)) for use in determining the jurisdictional threshold ratios has engendered substantial controversy. Some railroads have taken the position that this requires reliance upon broad-brush system average cost. On the other hand, a group of shipper complainants recently filed a petition for declaratory order with the Commission looking toward the determination of the actual variable costs of specific movements. Efforts have recently been made in informal meetings with the railroads to resolve this controversy but they proved unsuccessful and the issue is still pending. It may well become necessary for the Congress to consider clarifying legislation to spell out what we conceive to be the legislative intent to compare specific rates with underlying specific costs for jurisdictional purposes.

In conclusion, the Staggers Act has been given little chance to work since its enactment. The Commission has taken major steps to emasculate the limited right of captive shippers to invoke its jurisdiction or obtain warranted rate relief. The railroads, rather than exploiting enhanced rate-making flexibility over competitive traffic, have focused their major efforts upon increasing the subsidy from captive shippers by jurisdictional attacks and rate increases. The Congressional purpose of both the 4-R and Staggers Act of preserving jurisdiction to prevent possible monopoly abuse has been grievously subverted.

Appendix A

Middle South Utilities System
- Arkansas Power & Light Co.
- Louisiana Power & Light Co.
- Mississippi Power & Light Co.
- New Orleans Public Service Inc.

Cajun Electric Power Cooperative, Inc.
Central Louisiana Electric Co.
Gulf States Utilities Co.
Edison Electric Institute.

Senator Danforth. Thank you, Mr. Clark.

Mr. Loftus?

Mr. Loftus. Thank you, Mr. Chairman. Good morning, Senator Riegle. In my prepared statement, I have discussed several areas in which we believe there are problems with the Interstate Commerce Commission's implementation of the Staggers Rail Act. In the summary, I will confine my remarks to one point. That is market dominance.

During the legislative process which ended with enactment of the Staggers Act, the railroads attempted to change the standards for determining ICC jurisdiction to regulate rates to include consideration of geographic and product competition. These measures were rejected, first in the Senate and then in the House. In its final form, the Staggers Act retained the market dominance standard established in the 4-R Act for purposes of determining rate jurisdiction.

In July of this year, however, the Commission revoked its regulations for determining market dominance, and established a new set of guidelines which place major emphasis on consideration of geographic and product competition. We believe the Commission's new approach to market dominance is flatly inconsistent with the language and intent of the 4-R Act on market dominance, which was carried forward in the Staggers Act.

Let me hasten to add that not all railroads are similarly subject to criticism. Some make a diligent effort to cost out and eliminate losing business. It is more than a coincidence that these happen to be the more profitable members of the industry.

The two most fundamental problems with the Commission's new guidelines are that (a) the statutory definition of "market dominance" precludes consideration of geographic and product competition, and, (b) consideration of these issues defeats the statutory requirement of administrative feasibility.

The complexity of the evidentiary inquiry into geographic and product competition is enormous. In cases now being tried before the Interstate Commerce Commission under the new guidelines, the railroads are filing massive presentations concerning geographic and product competition, to which the shippers must respond in chapter and verse. The involved nature of these issues is reflected in the set of railroad interrogatories which I have appended to my prepared statement. Resolution of these issues will require lengthy antitrust-type proceedings before the Commission of a kind Congress clearly sought to avoid in the 4-R Act, where it directed the Commission to promulgate rules for determining market dominance "designed to provide for a practical determination without administrative delay" (202(B)—4-R Act).

The Commission's decisions establishing its new guidelines and revoking its regulations which were in effect as of the enactment of the Staggers Act are under appeal. If they are upheld, we believe that legislative action will be required to restore the market dominance concept to a reasonable, fair, and workable standard for determining the situations to which rate review jurisdictions should be extended.

Thank you.

[The statement follows:]

Statement of C. Michael Loftus

Good morning Mr. Chairman and members of the Subcommittee. I am appearing this morning on behalf of the American Public Power Association, the National Rural Electric Cooperative Association, the Western Coal Traffic League, and the Consumer Owned Power Coalition. Each of these organizations, which are described in Exhibit A to this statement, is vitally interested in matters affecting the rail transportation of coal and appreciates the opportunity to be heard this morning.

I am an attorney specializing in transportation law. My testimony is offered from the perspective of one who was involved in the legislative process which culminated in the Staggers Rail Act and has experienced on a day to day basis a number of the problems which have arisen in connection with the new law's implementation by carriers, shippers, and most importantly, the Interstate Commerce Commission.

Some of these problems have resulted from the Commission's actions in interpreting and applying the new law, and some from the Commission's failure to take action to resolve issues which have been raised by shippers or carriers as to the proper interpretation or application of the law. This statement will not attempt to deal with all of such problems, but will address several of the major areas where problems have arisen.

Jurisdictional Standards for Maximum Rate Regulation

(a) Market Dominance

The Staggers Act incorporates a number of provisions which were designed to afford the railroad industry new freedoms and flexibility in pricing and to reduce regulatory involvement by the ICC in rail ratemaking. Shipper interests generally, and coal shipping interests in particular, were deeply concerned that the effect of these provisions and other proposals which were contemplated in earlier versions of the legislation would be to deprive "captive" shippers of any opportunity to obtain ICC review of rates.

In fact, the need to preserve access to the Commission in order to protect captive shippers against unreasonable rates was the central issue in the Congressional debate on the Staggers Act and it was only after a compromise was worked out on

this issue that the measure was able to pass the House of Representatives. A central feature of this compromise was the retention in the law of the market dominance standard established in the Rail Revitalization and Regulatory Reform Act of 1976 ("4-R Act") as the basic jurisdictional test for rate regulation by the Commission.

The most serious problem which has arisen in the past year in connection with the Staggers Act is that the ICC has radically changed its entire approach to the market dominance jurisdictional standard. In the process, it has frustrated the carefully crafted compromise on the issue of rate review jurisdiction which was worked out in the legislative process.

In a proceeding known as Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations and Consideration of Product Competition, concluded in July, 1981, the Commission has adopted what it describes as "evidentiary guidelines" for determining market dominance which have transformed what had been a workable and fair jurisdictional standard into one which is hopelessly complex and burdensome. Simultaneously, the Commission revoked its regulations setting forth standards and procedures for determining market dominance which were promulgated pursuant to Congressional directive in the 4-R Act. Under those regulations, shippers were able to trigger a presumption that the carrier had market dominance where it could satisfy certain factural criteria reflecting the absence of competition. The regulations made no provision for the consideration of geographic and/or product competition in determining market dominance. First established in 1976, and upheld by the courts as being consistent with the requirements of the 4-R Act, these regulations were applied by the Commission in numerous cases and it was market dominance as determined under these regulations that was contemplated in the compromise that cleared the way for final passage of the Staggers Act.

The new evidentiary guidelines adopted by the Commission in July, 1981, differ radically from the regulations which existed at the time the Staggers Act was enacted in three principal respects. First, rather than establishing standards and criteria which a shipper can predict with a reasonable degree of accuracy whether it will be able to satisfy, the new guidelines are vague and unclear and have engendered tremendous uncertainty on the part of both shippers and carriers. Second, the new guidelines rely heavily on evidence concerning the existence of geographic and product competition. Third, largely as a result of the emphasis laid on geographic and product competition, the new guidelines allow and, indeed, encourage extremely complicated and lengthy evidentiary proceedings for determining market dominance. The net effect is that what was a relatively straightforward, administratively feasible, threshold test of jurisdiction is now a vague and confused standard requiring lengthy antitrust type proceedings. To give the Subcommittee some idea of the type of evidentiary issues which are raised under the new guidelines, a copy of a set of interrogatories dealing solely with market dominance issues is attached as Exhibit B.[1] These interrogatories, numbering 79 (most of which have multiple sub-parts) and covering some 45 pages, are typical of those now being served by the railroads upon shippers in cases before the ICC on the issue of market dominance.

The principal basis expressed by the ICC for its action in discarding its regulations and adopting the new guidelines was its belief "that Congress, in the Staggers Act intended a much more flexible interpretation" of the statutory definition of market dominance. (Ex Parte No. 320 (Sub-No. 2), supra 365 ICC, at 129). Far from providing any support for the Commission's new guidelines, the legislative history of the Staggers Act reveals that Congress specifically rejected provisions which would have included geographic and product competition in determining jurisdiction. In addition, the Conference Report made it perfectly clear that the market dominance definition was being retained unchanged:

The definition of market dominance under existing law has not been altered by the substitute and it is not intended that there by any change in the term . . . H.R. Report No. 96-1430, 96 Cong. 2d Sess. 88 (1980).

The Commission's decisions revoking the market dominance regulations and establishing the new guidelines are now under appeal in the U.S. Court of Appeals for the Fifth Circuit. Hopefully, the court will set aside the Commission's action and the regulations will be reinstated. If, however, the court affirms the Commission's decisions. legislative action will be required if the balance established in the Staggers Act between a) additional rate freedoms and other benefits for the railroads and b) preservation of ICC rate regulation jurisdiction as formulated in the 4-R Act and applied by the ICC as of the enactment of the Staggers Act, is to be restored.

[1] Exhibit B has been retained in the committee files.

b) Cost Determinations for Jurisdictional Thresholds

A somewhat technical but extremely consequential problem has arisen in a large number of cases before the ICC concerning the type of costs which can be utilized in determining whether or not the jurisdictional thresholds established under Section 202 of the Staggers Act have been satisfied. Railroads have argued that the relevant statutory provision, 49 U.S.C. § [illegible] should be interpreted as providing that the Commission may only look to "unadjusted" Rail Form A costs in determining whether the jurisdictional thresholds are exceeded, at least until the Commission itself prescribes specific adjustments for purposes of that provision. These unadjusted costs reflect the railroad's system average costs and may or may not have any relationship to the variable cost of the particular traffic. In most, if not all, of the cases where this argument has been raised, the shippers involved have submitted Rail Form A cost evidence which has been "adjusted" to reflect the characteristics of the actual traffic at issue. The railroads concede that these traffic-specific costs are appropriate for evaluating the reasonableness of rates but assert that under the language of the statute, the Commission must disregard such cost evidence and rely solely on unadjusted or average costs for determining jurisdiction. The net effect of adopting the railroad's interpretation of the statute would be to eliminate for all practical purposes, all ICC rate regulation for certain commodities such as coal because average costs for these commodities will very rarely exceed the jurisdictional thresholds, at least until such time as the ICC specifies cost adjustments to be applied for purposes of the thresholds.

Although this issue has been raised in literally hundreds of cases before the Commission, the Commission has yet to rule on the question. Recently, a petition for declaratory order was filed with the Commission requesting a resolution of this issue. It wold be very helpful if the relevant statutory provision could be amended to clarify that for purposes of applying the jurisdictional thresholds, variable costs shall be determined using the best cost evidence of record, be it evidence of unadjusted costs or evidence of costs calculated using adjustments which have been recognized and accepted by the Commission and the courts. In the absence of legislative clarification, it may be years before this technical issue is fully resolved.

REVENUE ADEQUACY

Next to access to the Commission for maximum rate regulation, the second principal concern of many captive shippers during the legislative process was that some of the extraordinary new rate freedoms contained in the Staggers Act were not necessary or appropriate for some carriers. Section 203 of the Staggers Act establishes a new zone of rail carrier rate flexibility which affords carriers extraordinary protections from regulatory involvement by the ICC in connection with certain rate increases. Thus, rate increases of up to six percent of an adjusted base rate may be taken during the first four years after enactment which, as a general rule, are not subject to suspension or investigation by the ICC. Beginning with the fifth year after enactment, the annual protected increase is four percent of the adjusted base rate.

The rate increases permitted under the rate flexibility zone are in addition to rate increases required to offset increased costs, i.e. they are by definition profit increases. The justification for affording these increases special protections from shipper challenge was that many carriers were sorely in need of increased revenues and only extraordinary measures such as the rate flexibility zone would permit them to increase their revenues to an acceptable level. Due to the efforts of Senator Long, the rate flexibility zone provision was amended to provide that consistent with its purpose, its use would be limited to carriers without adequate revenues. Thus, as Senator Long explained in his statement on the conference bill:

"Of primary concern to me that has been the need to insure that carriers which have already attained revenue adequacy are not allowed to bootstrap their requests for rate increases on captive traffic to the obvious needs of inadequate revenue carriers like Conrail or the Milwaukee. As long as inflationary cost increases can be recouped, there can be no rational justification, in my view, for a "revenue need" rate increase for any railroad that has been found to have achieved revenue adequacy.

"The Conference Bill would deny such revenue adequate carriers from taking advantage of the four percent rate flexibility zone of the bill. Also, for six percent rate flexibility zone, the ICC is to give due consideration, with view to preventing excessive profits on the traffic involved, to whether the carrier proposing the rate has adequate revenues."

Cong. Rec. S14003 (daily edition, September 30, 1980). The concept of revenue adequacy was also used in other sections of the Staggers Act to emphasize that the

trust of the new rate freedoms contained in the law was to enable financially weak railroads to achieve stability rather than to enrich those carriers which were already financially healthy. For example, Section 201 of the Staggers Act directs the Commission to recognize the policy that rail carriers shall earn adequate revenues when evaluating the reasonableness of individual rates.

In a rulemaking proceeding entitled Ex Parte No. 393, Standards For Railroad Revenue Adequacy, commenced in November, 1980 and concluded in March, 1981, the ICC has revoked the regulations for determining revenue adequacy which were in place as of the enactment of the Staggers Act and has instituted a drastically different method for measuring the adequacy of a carrier's earnings. The result of the Commission's decision in this proceeding is to defeat the Congressional intent in the Staggers Act that the revenue adequacy concept serve as a meaningful standard of differentiation between the nation's strong and weak railroads.

Under the standards and procedures in place at the time the Staggers Act was enacted, the ICC would look to all relevant financial indicators including flow of funds, rate of return on net investment and various ratios such as throw off to debt ratios and fixed charge coverage ratios in determining whether a rail carrier's revenues were "adequate" as contemplated under 49 USC § 10704(a)(2). Applying these standards, the Commission found in 1980 that 11 out of 31 Class I carriers possessed adequate revenues. Under its new approach, the Commission looks only to whether or not a carrier's return on net investment equals the current cost of capital. In adopting this standard, the Commission essentially disregarded a number of critical problems attendant upon utilization of a return on net investment standard for the railroad industry which had earlier caused it to reject this standard as a reliable indicator of the financial health of rail carriers. Applying its new standards, the Commission has found that only three railroads in the country (two of which are owned by U.S. Steel Corporation and one of which is a wholly-owned subsidiary of Burlington Northern) possess adequate revenues. Such carriers as Southern Railway, Norfolk and Western Railway, Union Pacific and others generally thought of as being financially solid enterprises are all deemed to have inadequate revenues.

The validity of the Commission's new standards for determining revenue adequacy is presently under appeal to the courts. If the Commission's decision is upheld, further legislative action will be required if the revenue adequacy concept is to serve, as it was intended to in the Staggers Act, as a means of distinguishing carriers in serious financial need from those carriers which are not. It should be noted that revenue adequacy is not utilized in the law as a limitation upon the earnings of carriers, but only as a measure for determining which carriers should have the benefit of some of the extraordinary new rate freedoms which the law now allows.

COST RECOVERY INDEX

Under Section 203 of the Staggers Act the ICC is required to publish a rail cost adjustment factor on a quarterly basis. The purpose of this cost adjustment factor is to measure the amount by which railroads' costs have increased so that carriers may be permitted to increase rates to recover such costs without any opportunity for shipper challenge. In effect, this feature of the Staggers Act serves to eliminate regulatory lag in the recovery of increased costs due to inflation.

The law provides that the cost adjustment factor shall be calculated using an index of railroad costs "which index shall be compiled or verified by the Commission, with appropriate adjustments to reflect the changing composition of railroad costs, including quality and mix of material and labor" 49 USC § 10707a(a)(2)(B). The Commission formulated this index in Ex Parte No. 290 (Sub-No. 2), Railroad Cost Recovery Procedures 364 ICC 841 (1981). The index adopted was based upon the Association of American Railroads' input price index with certain adjustments.

The Commission's implementation of this provision of the Staggers Act is deficient because the index which it has adopted provides to the carriers each quarter increases in revenue substantially greater than those required to recover increased costs. In other words, by overstating the level of cost increases, the cost adjustment factor enables the rail industry to increase profits, under the guise of strict cost recovery, every quarter.

The basic defect in the Commission's index is that it is an input price index, rather than a cost index as required by the law. In fact, language in the Senate bill tying the cost recovery factor to the AAR input price index was deleted in favor of language requiring the cost adjustment factor to be based on an index of railroad costs after extensive testimony to the effect that the AAR's input price index substantially overstated inflationary cost increases. See, e.g., Railroad Transportation Policy Act of 1979; Hearings on S. 1946 before the Senate Committee on

Commerce, Science and Transportation, 96th Cong. 1st Sess. at 434-37; 448, 451; 529. S. Rep. No. 96-470 96th Cong. 1st Sess. at 19-20, 52 (1979).

Because the index is based on input prices, it fails to take into account the effect of productivity on the extent of increased costs actually experienced by the rail industry and is thus contrary to the directive of the statute that the index "reflect the changing composition of railroad costs, including the quality and mix of material and labor" 49 USC § 10707a(a)(2)(B).

The Subcommittee will not be surprised to learn that the Commission's decision in Ex Parte No. 290 (Sub-No. 2) has been appealed to the courts. In the meantime, however, the railroad industry is attempting to capitalize on the Commission's decision by arguing in a recent filing at the Commission that it must change its long-established procedures for updating costs in order to be consistent with the methodology utilized for the cost recovery index. As the carriers have described this proposal, it would, in effect, raise the jurisdictional threshold for the numerous complaints filed at the ICC under Section 229 of the Staggers Act from 165 percent (in fact the applicable figure is 160 percent) to 184 percent of variable costs.

THE LONG-CANNON AMENDMENT

Under the terms of a provision which was authored by Senators Long and Cannon, the Commission is required, in determining whether a rail rate is reasonable, to consider several factors relating to the relative profitability of the different segments of traffic hauled by the carrier involved. Thus, the Commission must consider the amount of non-compensatory traffic hauled by the carrier, the extent to which the carrier maximizes revenues from marginal traffic and the mix of the carriers' traffic and whether particular segments of traffic are being required to pay an unreasonable share of overall revenues. 49 USC § 10707a(e)(2)(C). These criteria are similar to those identified by the Commission in coal rate cases decided prior to the Staggers Act, where the Commission found that carriers should be required to present evidence in these areas in order to justify any significant degree of differential pricing. The Commission is required to consider similar factors and also the impact of a proposed rate or rate increase on attainment of national energy goals in determining whether or not to investigate a rate increase which will result in a revenue/cost ratio more than 20 percentage points higher than the applicable jurisdictional threshold. 49 USC § 10707a(e)(2)(B). For example, during the twelve months ended September 30, 1981, this trigger point was 180 percent.

Consideration of these criteria is extremely important to captive shippers because it is these shippers that are asked to make up any revenue deficiencies or shortfalls which the railroads may experience in hauling competitive traffic. Only by considering such factors can the ICC determine whether the revenue shortfalls which captive traffic is being asked to offset through higher rates are (a) unavoidable (i.e., that they are not attributable to poor management on the part of the railroads)[2] and (b) fairly distributed among the various segments of traffic so that no particular traffic, such as coal traffic, is forced to pay an unreasonable amount of the additional revenues needed to offset the unavoidable revenue shortfall.

In the 13 months which have passed since enactment of the Staggers Act, there is no indication that the Commission has given any effect to the provisions of the Long-Cannon Amendment or even that it has any intention of doing so. Although the Commission has decided a number of cases during this period, only a very few have even made any reference to the criteria of 49 USC § 10707a(e)(2)(C). Similarly, although there have been a number of petitions requesting investigation by the Commission of rate increases where shippers alleged that the criteria of the Long-Cannon Amendment were triggered, there is not one instance, of which I, at least, am aware, in which the Commission has applied the criteria of 49 USC § 10707a(e)(2)(B) and issued the required statement of its reasons for investigating or refusing to investigate. Since Commission decisions in suspension matters are not subject to judicial review, there is little that a shipper can do to ensure that the Commission applies these standards. It may be that the evidence submitted in these various cases did not demonstrate that the Long-Cannon investigation criteria had been triggered, but it may also be that the Commission is simply ignoring this provision. This is a question which we believe merits this Subcommittee's consideration and we suggest that in pursuit of its oversight function, the Subcommittee should inquire of the Commission whether the provisions of 49 USC § 10707a(e)(2) (B) and (C) have been properly observed and if not, why not.

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[2] The statutory definition of revenue adequacy imposes a standard of "honest, economical and efficient management." 49 USC § 10704(a)(2).

TITLE III OF THE STAGGERS ACT—RAILROAD COST DETERMINATIONS

One of the few features of the Staggers Act which captive shippers looked upon as affording promise of fairer and more reasonable rate levels was the extensive emphasis placed upon the need to promulgate standards which would allow the determination of accurate railroad costs. Section 302 of the Staggers Act established a new Subchapter IV of Chapter III of Title 49 which created a Railroad Accounting Principles Board to promulgate appropriate cost accounting principles which would, once established, "govern the determination of all railroad costs for specific regulatory proceedings under this title." 49 USC § 11162(a). Another provision of this new subchapter, 49 USC § 11165, emphasizes the need to make relevant cost data available to shippers through the Commission's discovery procedures.

Although the law directs that the Railroad Accounting Principles Board shall complete the development of cost accounting principles within two years of enactment of the Staggers Act and shall report to Congress within such period concerning recommendations as to appropriate legislative or administrative action to implement such principles in regulatory proceedings, appointments have not been made to the Board because funds for its operations were never appropriated. As a result, this major aspect of the Staggers Act, which Congressman Florio described when introducing the bill in the House as "[o]ne of the most important features of this bill" (Cong. Rec. H.903, February 13, 1980), has simply died aborning.

Development of accurate costs has been a persistent and serious problem facing captive shippers because much of the data required to develop the actual costs for specific traffic movements is possessed solely by the carriers, which have frequently refused to produce it when requested under Commission discovery procedures. This problem has continued in spite of the enactment of 49 USC § 11165, basically because the ICC frequently refuses to compel the carriers to provide relevant information which has been requested.

It cannot be seriously questioned that all parties, shippers, carriers, and the Commission would benefit from the development and availability of accurate cost data. Unfortunately, the major initiative to advance this goal represented by Title III of the Staggers Act has been completely frustrated.

RAIL TRANSPORTATION CONTRACTS

One of the major features of the Staggers Act is the official statutory authorization of rail transportation contracts. This provision of the law has proven to be beneficial to both rail shippers and carriers in many situations. As had been anticipated, however, there has been very little contracting to date between the railroads and captive shippers such as utility coal shippers. We attribute this to two causes. First, captive shippers, by definition, have little or no leverage to bargain with a railroad to obtain fair and reasonable contract terms. Because the railroad in these situations has a monopoly over the traffic involved, it has no incentive to contract away the freedom it possesses in the absence of an agreement to increase rates at any time on twenty (20) days' notice. It is due to this situation that continued rate regulation by the Commission is required to protect captive shippers.

Secondly, there continues to be major uncertainty among railroads and shippers alike as to the nature of the standards which will be applied by the Commission in determining maximum reasonable rate levels. While this uncertainty continues, it is difficult for either party to commit to a long-term contract which could prove to be disadvantageous in light of the standards of rate reasonableness ultimately adopted by the Commission.

THE INTERSTATE COMMERCE COMMISSION

Although this statement has been repeatedly critical of the Commission's actions in certain areas crucial to an effective implementation of the Staggers Act, it should be recognized that the Commission has been operating under significant handicaps during the period since enactment of the new law. During this time when the Commission has been faced with a series of momentous rulemaking proceedings in connection with the implementation of the Staggers Act and the tremendous number of new cases filed under Section 229 of the Staggers Act, it has also experienced serious budgetary cutbacks and the loss of a significant number of its most experienced personnel. In addition, the composition of the Commission has been in a state of flux as various Commissioners have resigned or had their terms expire and new Commissioners have been appointed with the customary accompanying staff turnover.

In short, the Commission has been contending with a number of very difficult and complicated issues at a time of what appears to be considerable inner turmoil and

staff shortages, particularly in the ranks of the more experienced personnel. It is true that the Staggers Act and the 4-R Act before it were intended to reduce significantly the level of regulation imposed upon the rail industry, but both of these laws also acknowledge a continuing and critical need for the Interstate Commerce Commission. If the Commission is to be able to fulfill its continuing role under the Revised Interstate Commerce Act in an efficient and professional manner, it must be afforded resources in terms of budget and manpower which are commensurate with its duties. From the perspective of many practitioners before the Commission, it does not appear that this is the case at the present time.

We understanding that the Commission is presently funded for $74 million in fiscal year 1982. In order to enable the Commission to cope with the many challenges it currently faces, we hope that increases in this amount will be permitted for the next fiscal year, and we urge the Subcommittee to exert whatever influence it can to achieve this end.

Thank you again for the opportunity to appear.

Exhibit A

The American Public Power Association is a national service organization representing more than 1400 local, publicly-owned electric utilities in 48 states, Puerto Rico, the Virgin Islands, American Samoa and Guam. Local publicly-owned utilities serve approximately 14 percent of all U.S. consumers.

The National Rural Electric Cooperative Association is a national service organization whose membership consists of roughly 1,000 rural electric cooperatives. These members systems supply electricity to over 25 million people in 46 states.

The Western Coal Traffic League is a voluntary association of utility and industrial coal consumers whose members consume in excess of 25 million tons of coal per year. Because of the vital and continuing interest of its members in all matters pertaining to rail transportation of coal, WCTL has been an active participant in all major proceedings before the ICC affecting western coal transportation since its formation in 1976.

The Consumer Owned Power Coalition is a group consisting of the American Public Power Association, the National Rural Electric Cooperative Association, four other power service organizations and eighteen individual consumer-owned utilities and joint action power agencies. COPC was formed for the express purpose of participating in the rulemaking proceedings initiated by the Inerstate Commerce Commission in order to implement the Staggers Rail Act of 1980 and insuring court litigation.

[The following information was subsequently received for the record:]

Questions of Senator Long and the Answers Thereto

Question. We hear much about the necessity for differential pricing, or above full cost, pricing of so-called captive traffic. Are the shippers that you represent opposed to any such pricing?

Answer. As a matter of principle, not at all; and we have made that clear in specific cases. We believe, however, that before captive traffic is called upon to contribute through above full cost rates—which include Commission prescribed return—the Commission should both quantify the revenue shortfall and insure that the involved carrier is exercising due diligence to maximize the contribution from competitive traffic. At minimum, there can be no justification for requiring a captive shipper to make up for losses on traffic carried at an out-of-pocket deficit. A railroad shouldn't be permitted to compete for traffic that it can't attract at rates that at least cover variable costs, certainly not if their shippers are required to make up these losses.

Question. Doesn't the Act now provide for consideration of noncompensatory and marginal traffic and a fair apportionment of the contribution over all traffic?

Answer. Yes, sir, we consider that to be the essential thrust of the Long-Cannon amendment as now embodied in the Act. Unfortunately, however, we have seen no Commission implementation of those provisions, not even the development of data or evidentiary guidelines. On the contrary, the Commission has already applied in several specific cases a still pending proposal to change the method of allocating constant costs which one Commission decision recognizes as *de facto* differential pricing, without any undertaking to determine if the railroads involved have taken the necessary steps to improve the pricing of other traffic before being permitted to price differentially captive traffic.

Question. Are you saying that the Commission doesn't know how much money, if any, each railroad may be losing on noncompensatory traffic?

Answer. Exactly, at least not on a current or individual lines basis. As I noted in a footnote to my testimony, a 1977 1 percent waybill study indicated that the railroad industry had a deficit of $800 million from noncompensatory traffic.

Question. The major thrust of my efforts during the drafting of the bill was to insure that added rate freedom for the railroads was not achieved by depriving a captive shipper of the opportunity to seek relief from the Commission, and I believe that the Act confirms this approach. Are you now stating that the Commission has interpreted various provisions of the Act to curtail its jurisdiction beyond those envisioned by the Congress?

Answer. I am saying precisely that.

Question. One area in which I was personally involved also was to insure that rate zone increases to improve profits were to be confined to needy railroads. Do I understand that the standard of revenue adequacy we were dealing with at that time has been changed so as to classify as inadequate railroads that were previously deemed to be earning adequate revenues?

Answer. That is correct. Under the funds flow method used in the only determination made by the Commission prior to the Act, 13 Class I railroads were found to be revenue adequate. Now only 3 smaller roads are so classified under a cost of capital methodololgy. The Commission has changed the result through the simple expedient of changing the test.

Senator DANFORTH. Thank you very much. I am sorry to say we're in the last few moments of a rollcall vote now over in the Senate.

Senator Riegle, do you have any questions of this panel?

Senator RIEGLE. I do for Mr. Lundgren. I would like to just ask—I have three specific questions I would like him to respond to for the record. Let me submit those, and I'd ask that he answer those.

Senator DANFORTH. Mr. Lundgren, the Senator's questions will be submitted to you, and you can answer those for him.

Gentlemen, thank you very much. I will be back in about 10 minutes.

[(Recess.]

Senator DANFORTH. Next we have a shipper panel, consisting of Carl E. Bagge, James W. Lawson, Walter E. Morgan, and Donald G. Griffin.

Mr. Bagge?

STATEMENTS OF CARL E. BAGGE, PRESIDENT, NATIONAL COAL ASSOCIATION; JAMES W. LAWSON, ESQ., REPRESENTING NEVADA POWER CO.; WALTER E. MORGAN, CHAIRMAN OF THE LEGISLATIVE COMMITTEE, NATIONAL INDUSTRIAL TRAFFIC LEAGUE, ACCOMPANIED BY JOHN F. DONELAN, LEAGUE COUNSEL; AND DONALD G. GRIFFIN, REPRESENTING CHEMICAL MANUFACTURERS ASSOCIATION, ACCOMPANIED BY GLORIA SODARO, STAFF COUNSEL

Mr. BAGGE. Senator, on behalf of the coal producers of the Nation, in the 4 minutes allotted me I would like to make five basic points. We, the coal producers, supported the Staggers Rail Act, because we want a reliable railroad industry. We supported it on the theory that as captive shippers—it's been demonstrated that we are captive shippers; 85 percent of our coal is captive to rail—we thought that by cutting the point at which there would be oversight authority, 160 to 170, up to 180, ultimately, of the variable costs, that we would have some oversight afforded to us in the future. It was on that basis—on a finely tuned compromise a year ago—that we supported this bill.

We have to say today that the jurisdictional basis upon which coal would be afforded the benefit of oversight has been totally emasculated by the ICC. The fifth circuit is now litigating that point, because the Commission has interpreted the indicia of captivity in such a way as to make it virtually meaningless. We didn't know how greedy the railroads really would be, Mr. Chairman, when we effected this compromise a year ago, because the second thing that happened was that they filed a proceeding before the ICC to totally exempt from ICC jurisdiction all coal export rates. The implications of that, when we, as an industry, are attempting to respond to the international coal imperative—to completely exclude all export rates of coal—are quite ominous, we believe.

The next thing that happened was the emergence of the so-called Ramsey pricing principle—I think Senator Long's question to Bill Dempsey was a good one. That is to say the theory that the railroads can charge what the traffic will bear, where they enjoy a monopoly position with respect to captive coal shipments, is disastrous. We engaged the services of Fred Kahn, an eminent advocate of decontrol, who made his position very clear in the proceeding before the Commission.

So we had these three proceedings emanating from the Staggers Rail Act. We are very uncomfortable with the implications of each of them. We are here to say that in our view the only thing that Congress can do to really correct what's happening out there in the real world under the Staggers Rail Act is to accelerate the rate at which you provide Federal eminent domain authority for coal slurry pipelines. We believe the bottom line is that without the enactment, without bringing into play a competitive form of transportation, we're now facing railroad rates that far transcend anything we contemplated when this compromise was struck here in the Congress a year ago. We are also looking at increasing the rates on inland waterways for coal movements by virtue of the administration's bill to adopt the imposition of user fees on the waterways.

So we see that, in the final analysis, the only hope we have for coal shippers and coal users is the enactment of a slurry pipeline legislation. We think that the philosophy of decontrol of the railroads really requires the enactment by the Congress of Federal eminent domain authority for coal slurry pipelines, to provide a modicum of competition, to find some balance in coal rates, as we try to respond, as I say, to the international coal imperative and to the efforts of our society to shift increasingly away from imported oil and natural gas to coal in the utility and industrial sectors.

[The statement follows:]

Statement of Carl E. Bagge, President, National Coal Association

INTRODUCTION AND SUMMARY OF TESTIMONY

Mr. Chairman, my name is Carl E. Bagge. I am president of the National Coal Association. Our members are companies engaged in coal mining operations in all coal producing areas of the United States and other organizations associated with the U.S. coal industry.

In my testimony, I will show that railroads have substantial market dominance over coal traffic. Further, I will urge consideration in the Congress for legislative actions necessary to accomplish balanced implementation of the 1980 Staggers Rail Act, which we supported as signed into law 13 months ago. The new legislation we

request would not change the Staggers Act; rather, it would amend further the Interstate Commerce Act in order to assure that key provisions of the Staggers Act will be implemented in a responsible manner.

Railroads often represent the only practical way to move coal long distances. Last year more than 500 million tons of coal were carried by the railroads; nearly two-thirds of the 830 million tons of coal we produced in 1980. Coal represents about one-third of the total tonnage carried by Class I railroads; much more than any other commodity moved by rail. A study by NCA shows that 85 percent of the coal shipped on the railroads has no practical alternative available for long haul transportation. Clearly, coal shippers today are highly captive to the railroads.

We believe that the Staggers Act amended the Interstate Commerce Act in a manner which holds significant promise for achieving well-balanced railroad regulatory reform. We still believe that the Staggers Act is sound; but the same critical balance found in its passage is not present in subsequent regulations related to implementation of the Act.

As enacted, the legislation provides a foundation for fair and equitable treatment of both rail carriers and captive shippers. It furnishes important mechanisms which enable railroads to compete effectively with water, pipeline and motor carriers for movement of coal and other traffic in the interest of assuring a healthy railroad industry. But, recent experience has shown that the law must now be amended, not to change the Staggers Act, rather to be certain that all of the goals in the Act, including protection of captive shippers over which railroads hold market dominance, are realized.

We urge the Congress to move forward swiftly with legislation that would overcome certain deleterious actions the Interstate Commerce Commission has taken recently in regard to rail market dominance and the notion of exempting from regulation export coal traffic carried by the railroads, and with legislation that would clear away a serious barrier in the path of securing effective competiton for the movement of coal by facilitating the construction of coal slurry pipelines. Specifically, we urge the Congress to consider legislation which would:

Set forth in the law certain definitive and measurable conditions which shall determine the existence of rail market dominance over specific traffic, and thereby permit a captive shipper to seek timely relief from the Commission when monopolistic abuses are encountered in regard to rail rates and service;

Establish in the law that the Commission shall not exempt from regulation any non-contract traffic that is market dominant; and,

Provide federal eminent domain for interstate coal pipelines that are granted a certificate of public convenience and necesssity by the Interstate Commerce Commission.

More railroad transportation contract service should be utilized

The long standing, broad bond between coal and the railroads can be strengthened materially now that the Staggers Act, for the first time, explicitly authorizes rail carriers and shippers to enter into contracts for specific transportation service. My purpose in emphasizing contract service is simple. It is, after all, essentially non-regulated transportation service that can be arranged in a businesslike manner between private parties having a mutual interest in coal marketing and delivery systems.

The largest user of coal produced in the U.S. is the electric utility industry which consumes more than 70 percent of our annual coal production. Electric utilities must plan investments in facilities designed to burn coal, and must complete arrangements for dependable, long term supplies of coal for such plants, well in advance of initial deliveries. This means designing coal-fired boiler installations which match the properties of coal to be supplied, including heat value, volatility, ash and sulphur content, as well as ancillary plant equipment such as coal handling and storage facilities, three to four years before the first deliveries are made, in order to allow time for plant design, construction and testing to be completed.

Thus, electric utility coal supply contracts must be negotiated several years ahead of plant completion, and these agreements often have a duration of 25 to 35 years from the time the first coal deliveries are made. It is clear, therefore, that success in achieving greater use of coal, our most abundant energy resource, can be significantly enhanced if the movement from the mine to an electric utility plant is both contractually assured and acceptably priced for extended periods of years. With this in mind, railroad transportation contract service represents a desirable approach to assure that coal secured under long term supply agreements also is covered by matching transportation contracts and will be on hand at electric utility plants in planned quantities at predictable delivered prices on a long term basis.

Until the Staggers Rail Act of 1980 was enacted, a question existed as to the lawfulness of railroad transportation service contracts in regard to whether dedication of certain rail carrier manpower, equipment and facilities to specific traffic violated its common carrier obligation. The Staggers Act removes any uncertainties about the lawfulness of contract services; one of the key aspects of the legislation that we found to be most desirable, influencing our decision to support the Act. The National Coal Association long has advocated the use of contract service, and has supported the notion of allowing rail carriers to operate both as common carriers and as contract carriers, in the latter sense essentially in a non-regulated fashion. We, therefore, welcome a recent trend toward more contracting for coal movement between rail carriers and shippers. More than two dozen railroad transportation service contracts have been entered into for movement of coal produced in eastern, central and western coal-producing states to consumers in the U.S. and to ports for overseas export of U.S. coal since the 1980 Act was signed into law 13 months ago. This is regarded as a positive sign that the 1980 Act works in part.

NCA is gravely concerned about three recent actions by the Interstate Commerce Commission

However, we are gravely concerned about three recent actions by the Interstate Commerce Commission which have grievous implications for coal, and are likely to subvert the notion of contracting for railroad transportation service because they create a serious disincentive for railroads to enter into negotiations with captive shippers on coal traffic service. These actions are identified under proceedings: Ex Parte No. 320 (Sub-No. 2) 346 (Sub-No. 7), and 347 (Sub-No. 1) before the Interstate Commerce Commission.

The Commission's decision to wipe out rational tests for determining rail market dominance is wrong and must be corrected immediately

Our belief that the 1980 Act represents a balanced approach to fair and equitable railroad regulatory reform has been shaken substantially by the Commission's recent decision to wipe out long standing, rational tests for determining whether certain traffic is rail market dominant, and therefore entitled to seek relief from the Commission when a captive shipper encounters monopolistic abuses in terms of excessively high rail rates or inadequate transportation service due to the shipper's vulnerability to dominance in the hands of a carrier. This decision of the Commission under Ex Parte No. 320 (Sub-No. 2) is wrong, is contrary to the overall goals of the 1980 Act which include captive shipper protection, and must be corrected immediately so that responsible implementation of the Act can proceed as intended.

NCA filed comments citing the errors contained in the Commission's proposals at several stages of this proceeding prior to the decision to eliminate previous tests for determining the existence of rail market dominance. We were ignored by the Commission; and now, much to our dismay, we find ourselves in litigation against the Commission and its decision served on July 8, 1981 becoming effective 30 days thereafter. NCA presently has standing as an intervenor in litigation before the U.S. Court of Appeals for the Fifth Circuit which seeks to correct the problem created by the Commission in its decision to wipe out rational tests for determining market dominance; a decision which blatantly disregards the 1980 Act's provisions on captive shipper protection by making a showing of market dominance virtually impossible. We did not believe that our support for effective, balanced railroad regulatory reform through the 1980 Act would ever be so casually subverted by the Commission through the abrogation of its responsibility to furnish timely, positive recourse for captive shippers when they encounter monopolistic abuses, as the Commission has shown by its July 8, 1981 decision on rail market dominance.

Now we must urge that the previous, straightforward presumptions of market dominance be reinstated; namely, the high railroad market share (70 percent) test, the substantial shipper investment in rail-related facilities test, and the revenue (rate)-to-variable cost test adjusted somewhat to reflect the jurisdictional thresholds which are established under the 1980 Act. Otherwise, imprecise and highly arbitrary guidelines stated by the Commission in its July 8, 1981 decision which became effective August 7, 1981 will continue to replace rational and acceptable standards which are measurable and can be used in a timely fashion in decisionmaking on the existence of competition for traffic in question. The Commission's new guidelines rely on consideration of some thirty factors bearing generally on the existence or absence of effective competition upon which it says it will be willing to receive evidence.

The effect of the new guidelines is to compound greatly a shipper's burden in making a showing of market dominance. The gist of the Commission's guidelines is whether commodities involved could have been acquired from different sources

using other carriers or whether other commodities could have been substituted for the traffic in question, again carried by different carriers. Such evidentiary guidelines on geographic and product competition would cause the earlier definitive presumptions of market dominance to be replaced by a full blown adjudicative proceeding to determine market dominance, lacking even tentative benchmarks for decisionmaking. They ignore the fundamental issue of basic relevance; that is, could the traffic be moved practically using other transportation than provided by carriers alleged by shippers to represent the only viable supplier of transportation for a movement.

NCA urges the Congress to consider legislation on market dominance

We urge the Congress to consider swiftly legislation which would amend the Interstate Commerce Act further in order to establish in a definitive manner, the conditions under which traffic is found to be subject to market dominance. NCA suggests that three conditions would be appropriate for this purpose: the shipper has substantial capital investment in rail-related plant(s) or equipment for the movement; or the railroad(s) carry 70 percent or more of the traffic at issue; or the ratio of revenue-to-variable cost is higher than five percentage points above the jurisdictional threshold ratio presently in effect pursuant to the 1980 Act.

We believe that these conditions accurately and reasonably set out circumstances under which a movement is rail market dominant; and, if any one of the three conditions exist, the shipper should have ready access to the Commission for relief from rates that are excessively high for the service provided or from inadequate levels of service.

NCA further urges the Congress to consider legislation on exemptions

An issue of similar concern to the recent decision on rail market dominance is the Commission's consideration of a proposal to exempt from regulation export coal traffic carried by railroads to the East, Gulf and West Coasts of the U.S. A proceeding, Ex Parte No. 346 (Sub-No. 7), has been instituted by the Commission following the petition of several coal-carrying railroads in which the Commission will decide whether export coal traffic should be exempted from regulation as now possible under Title 49, United States Code, as amended by the 1980 Act. This notion constitutes a serious effort to undercut in a grievous manner, the captive shipper protection afforded in present law.

It represents a gross misuse of the statutory exemption provisions in the law previous to the Staggers Act, and as amended by the Act last year. The Conference Report to the Staggers Act makes clear that the Congress has recognized that coal is captive to the railroads and should be subject to regulatory protection against monopolistic abuses in rates and service. It is almost inconceivable that one of the first applications to the Commission to take advantage of the exemption provision in present law is for export coal movements.

NCA studies show that 85 percent of the coal carried by the railroads has no practical alternative transportation available. Trucks are not economic or energy-efficient for long haul movements of heavy tonnages of coal or other similar bulk commodities. Water transportation is not possible in many instances due to the absence of navigable waterways. And, coal slurry pipelines are not yet in place, except for one installation in the southwestern portion of the U.S. There simply is a serious lack of competitive transportation for much of the coal produced in the U.S. Indeed, export coal is especially subject to rail market dominance, since not only must the coal be shipped by railroad from the mine, it also is almost always loaded aboard ocean vessels at railroad-owned port terminals.

It is not credible to assert, as the railroads do, that regulation of coal movements is unnecessary to prevent abuse of market power they hold. It plainly would be a miscarriage of the statutes to exempt export coal. Should an exemption be granted as now considered by the Commission, rail carriers would not be required to meet common carrier obligations for a classic example of captive traffic, export coal, a circumstance that we consider intolerable and not in the national interest. We also wonder if this potential abrogation of Commission responsibility is but a signal that other captive coal traffic, other export commodity movements such as grain, fertilizers, and chemicals, and rail movements of most bulk commodities whether for export or for domestic terminations, would also face prospective loss of captive shipper protection. This certainly is not in conformance with the intent of Congress in enacting the Staggers Act.

For the reasons previously given, and with the current propensity of the Commission to disregard its responsibilities with respect to captive shippers in mind, we urge the Congress to consider legislative action which would prohibit the Commission from exempting from regulation pursuant to Title 49, United States Code, any

rail market dominant traffic as determined by any one of the three tests that I have stated earlier except rail traffic carried under contract service which is essentially non-regulated under present law as amended by the Staggers Act. To exempt captive traffic from regulation is an unmistakable circumvention of the 1980 Act; the ongoing effort to exempt export coal traffic thus requires prompt, decisive action by the Congress to avert further consideration of the errant proposal now before the Commission.

The Interstate Commerce Commission must recognize that cross subsidization is wrong

The Commission, in a pending proceeding on nationwide railroad coal rate guidelines, Ex Parte No. 347 (Sub-No. 1), is considering a new scheme under which coal would be called upon to contribute a much higher amount of a rail carrier's revenue for meeting its fixed costs. Essentially, the question in this proceeding is how to allocate fixed costs among shippers. The Commission is seen to be leaning strongly to cost allocation methodology that would place too high a share of railroad fixed costs on captive coal traffic.

The Commission begins with the notion of differential pricing and carries this to a conclusion that it would prefer to place the largest share of railroad fixed costs on the shippers most captive to the railroads, that is, coal shippers. This approach clearly leads to extensive cross subsidization of other rail traffic by coal, a scheme that the Commission must realize is wrong, and inconsistent with the 1980 Act.

To replace allocation methodology where fixed costs are allocated based on the ratio of revenues generated by the traffic to total revenues, the Commission proposes to utilize its so-called ton-and-ton-mile formula which would place a large share of railroad fixed costs on coal traffic because of its weight and long haul characteristics. We opposed the proposal, on which a decision is still pending. Our fundamental argument is that it would be contrary to the 1980 Act for the commission to adopt a standard requiring coal to subsidize other rail shippers.

In contrast, we proposed an avoidable cost methodology which would have the Commission do a better job of identifying those costs that are attributable to particular traffic, reduce the unallocated cost pool, and assure that both competitive and non-competitive rail traffic is required to contribute sufficient revenues to cover their legitimate share of railroad fixed costs. Thus, cross subsidization is avoided, and the 1980 Act's directive to eliminate non-compensatory traffic is suitably accommodated.

On the other side, the railroads challenged the adoption of the Commission's proposed ton-and-ton-mile methodology for allocating railroad fixed costs for different reasons. They said that it would produce too low rail rates for carrying coal. Instead, the railroads proposed the adoption of "Ramsey pricing", a form of demand-based pricing whereby shippers who are more captive would pay a greater portion of railroad fixed costs than others having competitive alternatives. Clearly, coal is a target for the railroads' approach to capturing higher revenues. NCA has asked the eminent Cornell University economist, Dr. Alfred E. Kahn, to analyze the railroads' proposal. Among Dr. Kahn's findings and conclusions, he makes four key observations:

First, the implicit assumptions of railroad economists that unrestricted "Ramsey pricing" is necessary so long as a railroad fails to earn the current cost of capital on its entire net invested capital is questionable;

Second, the railroads' apparent assumption that principles of economic efficiency require captive shippers to contribute to a return on railroad facilities that do not serve them is not valid;

Third, "Ramsey pricing" on the basis of differences in demand elasticity of various groups of customers that are attributable to the presence or absence of intramodal competition raises serious questions—which the railroads have not confronted—about both economic efficiency and fairness; and

Fourth, the railroads should not be permitted the unrestricted exploitation of captive coal shippers entailed by unconstrained "Ramsey pricing" so long as they continue to restrict competition by obstructing the entry of coal slurry piplines into the transportation market.

To provide effective competition for coal movement, federal eminent domain should be granted coal slurry pipelines

This leads to an obvious and basic question of how to enable greater competition for coal movement so that market forces can be called upon to keep coal transport rates reasonable and stimulate the transportation industry toward constant efforts to increase the efficiency of coal movement and thereby hold down transport costs. The answer is simple. Construction of coal slurry pipelines should be encouraged

and facilitated by granting federal eminent domain, an important factor in the acquisition of essential rights-of-way for this proven, economic, and user-paid-for coal transportation system.

We urge the Congress to move quickly in considering legislation which would provide federal eminent domain for interstate coal slurry pipelines that are granted a certificate of public convenience and necessity by the Interstate Commerce Commission through an expeditious procedure for handling applications submitted to the Commission for its consideration. Such legislation has been introduced in the House of Representatives. A bill, H.R. 4230, the Coal Pipeline Act of 1981, is now under consideration by the House Committee on Interior and Insular Affairs. Mr. Chairman, I have included a copy of my testimony before the House Interior Committee on July 30, 1981 with the statement prepared for presentation at this hearing. I respectfully request that the July 30, 1981 statement be incorporated with my testimony and made part of the record for this hearing.[1]

We strongly support H.R. 4230 as introduced in the House of Representatives, and urge that similar legislation be considered by the Senate at this time. The pending legislation provides that, in order to have eminent domain for right-of-way acquisition, a proposed pipeline must receive certification by the Commission under procedures which assure that all interested parties have ample opportunities to be heard. We believe that federal eminent domain for interstate coal pipelines now properly is within the responsibilities of the federal government and represents a critical factor in accomplishing greater use of coal, our most abundant energy resource. U.S. coal producers already are broadly and intensively competitive in the supply of coal from mines in all coal-producing areas of the U.S. Now we need better competition among coal transporters to let market forces fully interact toward keeping the delivered price of coal reasonable—an important strategic goal of great benefit to the consumers of energy.

The 1980 Act has given the railroads a valuable mechanism for competing effectively with other transport systems, including pipelines. The lawfulness of railroad transportation contract service is now clear. The railroads can contract for coal shipments over many years, thus the rail carriers are in a good position to compete for coal traffic with slurry pipelines. The major thrust behind the 1980 Act was to make our railroads more competitive in the transport sector of our economy. This has been achieved. Now we should move ahead with legislation that will enable competition for coal traffic to be facilitated by granting coal slurry pipelines federal eminent domain. No public monies are needed, no federal programs are created, and no subsidization is required for this purpose. Surely, we should no longer delay passage of such vital and timely legislation.

Mr. Chairman, I have concluded my testimony, and would be glad to respond to questions. Thank you for allowing me to present the views of the National Coal Association on the implementation of the 1980 Staggers Rail Act.

Senator DANFORTH. Mr. Lawson.

Mr. LAWSON. I speak on behalf of the Nevada Power Co., an electric utility located in Las Vegas, Nev. Nevada Power made its commitment to convert to coal in 1963. It went on line with its first coal-fired generation station in 1965, and has proceeded to augment those over the years. Nevada Power has been faced with ever-escalating coal freight rates, and believes that certain provisions of the Staggers Act may be inconsistent with our national transportation and energy interests.

The enormous rate of return for transportation of captive coal at jurisdictional threshold levels and the availability of differential pricing to establish coal transportation rates at even higher levels to make up revenue shortfalls due to depressed rate levels on intermodally competitive traffic, may impact adversely on both energy interests and the general economy. We have calculated with respect to our delivering carrier that the jurisdictional threshold of 160 percent in the Staggers Act will bring a rate of return on investment of 30 percent to the carrier, pretax, and on stockholder's equity of 44 percent, and that the returns on the maximum

[1] The material referred to has been retained in the committee files.

threshold after a 4-year period of 180 percent would be 43 percent and 65 percent, respectively.

I submit to you that this is black gold, if you please, and the railroads will take as much of it as they can. We believe that the problem is that because of the ability of the railroads to extract huge price markups from captive shippers in the absence of regulation, the ICC and the railroads have both viewed the cost percentage jurisdictional thresholds as a rate floor rather than a rate ceiling.

The ICC has therefore continued to cast about for means to rationalize higher rates above full cost. They did this with the 7 percent additives. They did it with the ton/ton mile cost allocation. But it's never enough. The railroads continue to test the waters. They continue to cry poor mouth when they're making enormous rates of return for the transportation of coal. Their problems—if they have problems—are in other areas than in the transportation of coal.

Finally, I would like to say something with respect to two basic procedural problems. The ICC has adopted a practice of proposing major changes in their ratemaking criteria in notices of proposed rulemaking, and then proceeding to implement those changes resulting in higher rate levels in individual ratemaking cases prior not only to ultimate resolution, but also prior even to receiving comments in the rulemaking proceedings themselves. And I have given some examples in my prepared remarks of their doing this.

The interlocking and bootstrapping of cases unduly burdens shippers by requiring them to cover all bases in order to protect vital interests. Moreover, the implementation of changes in ratemaking proceedings which are being concurrently proposed but have not yet been approved in rulemaking proceedings is a radical departure from sound regulatory principles.

Thank you.

[The statement follows:]

Statement of James W. Lawson, Attorney

I. INTRODUCTION

I am an attorney admitted to practice in the District of Columbia, Maryland and Missouri.

This statement is submitted on behalf of Nevada Power Company, Las Vegas, Nevada, which operates a coal-fired generating station at Moapa, Nevada that receives 1,000,000 tons of coal per year delivered by the Union Pacific Railroad Company, which is originated by the Utah Railway Company at Hiawatha, Utah nd the Denver and Rio Grande Western Railroad Company at Acco, Utah.

Commencing in 1982 Nevada Power will receive at Moapa an additional 1,000,000 tons per year of coal from Utah, due to an increase in plant capacity. This projected annual volume of two million tons could possibly be tripled or quadrupled if the Allen Warner Valley project is not revived and the proposed Harry Allen station should receive by rail. My remarks are based upon experience in rail rate and rulemaking proceedings before the ICC and court appeals in which I have represented Nevada Power Company.

II. IMPLEMENTATION AND EFFECTS OF STAGGERS RAIL ACT OF 1980

A. *General*

The Staggers Rail Act of 1980 has resulted in an unprecedented rash of litigation before the I.C.C. and the Federal courts. The Section 229 "Savings Provisions" have provoked more than 800 formal complaints filed before the ICC. The new standards set forth in the Staggers Act have engendered a large number of rulemaking

proceedings within a short period of time which have taxed to the extreme the resources of consultants, attorneys, and parties in order to make timely and meaningful comments. The I.C.C. has undoubtedly been overcome by the avalanche of paper work; and its rulemaking decisions, heavily slanted in favor of railroad interests, have generally been characterized by absence of meaningful discussion of the representations of the parties, and rationalization of arguments in support of its actions, rather than consideration of facts, law and sounds economic and regulatory principles. The notices of proposed rulemaking issued in the early days following the passage of the Staggers Rail Act of 1980 were issued by an I.C.C. still hell-bent on de facto deregulation, self destruction, and favoring the railroads without regard to other public interests and considerations. Those proposals were predicated upon rationale enunciated by its Office of Policy Analysis, which was little more than an internal mirror of policy developed by the AAR. Through interlock and bootstrapping of the rulemaking proceedings shipper interests have multiple opportunities to lose on many issues. To the extent that decisions have been issued in the various rulemaking proceedings, such decisions are the subject of court appeals.

B. Specific

Specific sections of the Staggers Act which have presented problems or raised questions are:

1. *Section 2.—Findings.*—The finding that "by 1985, there will be a capital shortfall within the railroad industry of between $16,000,000,000 and $20,000,000,000" has been seized upon by the Commission as major justification for actions or proposed actions, without giving adequate consideration to the specific requirements set forth under Section 101(a)—Rail Transportation Policy, with respect to which the Conference Report states:

The new section establishes a specific rail transportation policy to guide the Commission in its duties in regulation of the railroad industry. The Conferees intend that this policy include the encouragement and promotion of the transportation of coal by rail in accordance with the objective of energy independence at rates which do not exceed a reasonable maximum where there is an absence of effective competition. [p. 80]

The I.C.C. minimized the effect of any of its actions upon energy matters in stating in its Notice of Proposed Guidelines in Ex Parte 347 (Sub. No. 1) Coal Rate Guidelines—Nationwide served November 18, 1980:

13 According to the recent report of the World Coal Study, oil at $35 per barrel is equivalent to coal at $165 per ton. Assuming a $45 average delivered price of coal, and allowing $35 per ton for complete pollution control, the cost of oil exceeds that of coal by some $85 per ton, on a BTU-equivalent basis. Under no assumptions would the rates under consideration in this proceeding remotely approach an $85 per ton increase over current rates. (See Carroll L. Wilson et al, Coal—Bridge to the Future, Ballinger, 1980.) [p. 29]

The Commission's treatment of energy consideration appears to be a carry-over from DOT's advocacy that the railroads be allowed to capture the differential between the BTU delivered price of domestic coal and foreign oil.

The I.C.C. has completely missed the point of energy economics. It is at the economic margins that all decisions are made so that any reduction in the presumed attractiveness of coal versus oil would result in some adverse energy decisions.[1]

No one has ever considered the economic or energy consequences of cross-subsidization which inheres in the economic tax on captive coal moving at the statutory jurisdictional thresholds. Will the movement of coal at these thresholds save Conrail? Is Conrail worth saving? Is it appropriate that other railroads take down enormous profits on coal rates set at jurisdictional thresholds designed to save Conrail? What does this do to energy policy? What does this do to coal producers? Coal miners? Exports? Balance of payments?

How much of the alleged $16–20 billion capital shortfall still exists? How much will be remedied by recent changes in the tax laws, including provisions for sale of tax write-offs and approval of railroad depreciation of assets for tax purposes? How much of the shortfall is attributable to Conrail? How much to the coal-carrying railroads which, for the most part, are very healthy?

Band-aids for Conrail may wreck havoc elsewhere and fail to save Conrail.

It is essential for reconciliation of our national transportation, energy, and fiscal interests that a data-oriented economic study be initiated so that decisions may be made on the basis of facts and economic principles, rather than rationalizations. This study should probably be independently commissioned.

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[1] See Comments of Nevada Power Company in Ex Parte No. 347 (Sub. No. 1).

2. *Section 201—Regulation of Railroad Rates.*—In Ex Parte No. 355, Cost Standards for Railroad Rates[2] in implementation of its responsibility to set minimum rate standards, the Commission has established standards that would allow the carriers to set rates so low on competitive traffic that traffic handled at such rate levels would have to be subsidized by captive traffic. Curiously, the Commission has also apparently utilized flow-through of investment tax credit in this proceeding so as to further depress minimum rate levels while in Ex Parte No. 347 (Sub No. 2), Coal Rate Guidelines—Nationwide[3] the Commission proposes to retain deferred taxes in the rate base, which is what it has done in its decision in Ex Parte No. 393, Standards for Railroad Revenue Adequacy.

3. *Section 202—Determination of Market Dominance.*—This section poses a whole host of philosophical and interpretive problems.

First and foremost is the problem that it places a premium on inflation of variable costs, thereby reducing the ratio of rate to variable costs, so as to diminish regulatory jurisdiction.

In Ex Parte No. 399, Cost Recovery Percentage, the I.C.C. proposes to use procedures which would improperly distort and inflate the cost recovery percentage which ultimately will be used as the jurisdictional threshold. The Commission had done this by several means. First, it has indiscriminately used the Kearney Study which was thoroughly discredited in Ex Parte No. 320 (Sub No. 1), Rail Market Dominance and Related Considerations, where the Commission warned about technical limitations in the Kearney Study with respect to data errors and omissions, sampling accuracy and that "revenue-cost ratios on coal movements are misleading." In Ex Parte No. 355 the Commission disavowed the Kearney Study where its use would have resulted in higher minimum rates than the Commission ultimately decided.

Notwithstanding, the I.C.C. in Ex Parte No. 399 used the Kearney Study to inflate the maximum rates allowed, attaching a portion of the Kearney Study as an appendix to its notice significantly omitting, however, the caveat "file contains errors." In other words, the I.C.C. uses or refuses use of the Kearney Study depending on whether its purpose is to inflate maximum rates (Ex Parte No. 347) or decrease minimum rates (Ex Parte No. 355). This typifies the perversity of the I.C.C.'s rule-making proposals. Second, the Commission improperly included noncompensatory traffic. Third, the Commission arbitrarily excluded other traffic. The Commission's initial notice indicated that it intended to use the ton/ton-mile methodology and allow deferred taxes to remain in the rate base which it had merely proposed, but had not finally approved, in other proceedings. In its further notice, the Commission failed to indicate whether it had in fact implemented those proposals.[4]

In Ex Parte No. 320 (Sub No. 2), Market Dominance Determinations and Consideration of Product Competition, the I.C.C. has very strangely abandoned its previous procedures for determination of market dominance which involved three fairly well-defined rebuttable presumptions with respect to market share, ratio of rate to cost, and substantial shipper investment, and instead substituted considerations of product and geographic competition. More strangely, it has adopted these vague and troubling concepts after having professed difficulty in applying the fairly well-defined pre-existing presumptions. Strangest of all, it has injected product competition into market dominance determinations in the face of the express prohibition against doing so in § 205 of the Staggers Act. It did correctly disavow that which § 205 would allow, but not require, namely consideration of product competition with respect to rate reasonableness.[5] Product competition is not an appropriate consideration for either market dominance or rate reasonableness.

The increasing jurisdictional thresholds will result in such an enormous rate of return on captive traffic as to suggest that this effect was either unknown or not understood by Congress at the time of enactment of the Staggers Act.

For example, a revenue to variable cost ratio of 148.8 percent would yield sufficient revenues for the Union Pacific Railroad Company to cover total cost at 1980 expense levels, including the Commission's calculated current cost of capital of 19 percent before tax. The level of return would be even higher at this revenue/cost ratio if actual tax rates and cost of debt were utilized. The UP at a revenue to variable cost ratio of 160 percent would generate a return before tax of 24.74 percent or a 30 percent increase above that currently deemed reasonable by the

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[2] 362 ICC 800, 812 (July 9, 1980), as modified at 364 ICC 898 (May 12, 1981).
[3] See Comments of Nevada Power Company filed May 11, 1981.
[4] See Comments of Nevada Power Company, dated March 16 and June 8, 1981.
[5] See Comments of Nevada Power Company filed February 17, 1981.

Commission (19 percent). The pre-tax return on equity would be 34.57 percent or 38 percent higher than the 25 percent level deemed reasonable by the I.C.C. The after tax return on stockholders' equity would be 18.67 percent, or 38 percent greater than that currently utilized by the Commission. The UP at a revenue to variable cost ratio of 180 percent would generate a return before tax of 34.97 percent, or an 84 percent increase above that currently deemed reasonable by the Commission (19 percent). The pre-tax return on equity would be 51.62 percent, or 106 percent greater than the I.C.C. level deemed reasonable. The after tax return on stockholders' equity would be 27.88 percent, or 106.5 percent greater than that currently utilized by the Commission.

If the allowance for deferred taxes is removed from the investment base, the UP would only be required to have a revenue to variable cost ratio of 141.6 percent in order to earn the I.C.C.'s determined 19 percent rate of return. At 160 percent of variable cost, the return on investment before tax would be 30.66 percent, or 61 percent greater than that deemed reasonable by the Commission. The return on stockholders' equity before tax would be 44.43 percent, or 77 percent higher than that deemed reasonable by the Commission. At 180 percent of variable cost, the return on investment before tax would be 43.34 percent, or 128 percent greater than that deemed reasonable by the Commission. At 180 percent of variable cost, the return on stockholders' equity before tax would be 65.56 percent, or 162 percent higher than that deemed reasonable by the Commission. From this it can be seen that even assuming the statutory tax rate of 46 percent and a current cost of capital, including the current cost of debt, the UP would be earning a substantial subsidy at any of the jurisdictional thresholds contained in the Staggers Act.[6]

These figures are provided with respect to the UP because they are readily available as concretized examples of the enormous return the jurisdictional thresholds will generate, and the enormous burden they will place upon captive traffic. Notwithstanding these enormous rates of return generated by, and burdens placed upon, captive traffic as the jurisdictional threshold is phased upward over a four-year period from 160 to 180 percent, the Commission plunged ahead with its proposals in Ex Parte 347 (Sub No. 2) Coal Rate Guidelines—Nationwide for new methods of maximum rate determinations which would eclipse even these extraordinarily high jurisdictional thresholds established by Congress.

Thus, by adoption of the ton and ton-mile method of allocation of constant costs and inclusion of deferred taxes in the rate base the Commission would set maximum rate levels far in excess of the jurisdictional thresholds. For example, compare the revenue or rate to cost relationships in various western coal cases of the fully allocated cost, dollar ratio (FAC, DR) and ton/ton-mile (FAC, T&TM) method of allocation of constant costs with the I.C.C. prescribed rates which have mostly been reversed on appeal:

Line No.	Coal case	Percent		
		FAC, DR	ICC prescribed rate	FAC, T. & T.M.
	(a)	(b)	(c)	(d)
1	SWEPCO	159.0	170.1	215.0
2	Council Bluffs	168.2	179.9	224.8
3	Sergeant Bluffs	159.9	171.1	223.3
4	Kings Mill	170.8	203.1	224.0
5	San Antonio III	158.1	169.2	182.1
6	Smithers Lake	NA	175.1	222.6
7	Arkansas P. & L	169.9	176.3	204.0
8	Acco	147.8	180.3	180.3

As can be seen in the above table, under FAC, DR the revenue-to-variable cost ratios range from 147.8 percent to 170.8 percent. Under the I.C.C. prescribed rates, the revenue-to-variable cost ratios range from 169.2 percent to 203.1 percent. Howev-

[6] Opening Statement of Facts and Argument of Nevada Power Company on Reopening filed November 9, 1981 in I.C.C. Docket No. 37038, Bituminous Coal, Hiawatha, Utah to Moapa, Nevada.

er, under FAC, T&TM there is a much higher revenue-to-variable cost ratio range, i.e., from 180.3 percent to 224.8 percent.[7]

Since the Commission would automatically apply ton and ton-mile methodology in determination of maximum rate levels, the Staggers Act jurisdictional thresholds would become meaningless. For, with respect to captive traffic, automatically applied maximum rate levels tend in almost all cases to become also the minimum rates or rate floors upon which the carriers attempt to build new justifications for increases.

In case the Commission's proposed ton and ton-mile methodology, which it has already implemented in Nevada Power's Acco case, somehow fails to be sustained, other methods, lie lurking in the wings to escalate the jurisdictional thresholds administratively. For example, the railroads have proposed in a petition filed in Ex Parte 411 to revise the cost updating methodology of the Commission in accordance with Ex Parte 290 (Sub No. 2) resulting in an increase in the jurisidictional threshold by some 20 points. In case this fails, there is of course the proposal for conversion from Rail Form A costing methodology to URCS, the Uniform Rail Costing System, which would likewise have the effect of inflating the jurisdictional threshold by some 20 points.

All of these proposals run contrary to the legislative intent.

Adoption of ton/ton-mile costing, or any device for peremptorily inflating the jurisdictional threshold, would negate the entire regulatory scheme of the Staggers Act, namely that the I.C.C. exercise maximum rate jurisdiction on captive traffic at and above the jurisdictional threshold of 160 percent. This threshold of 160 percent was adopted by Congress at a time when the I.C.C. was utilizing dollar ratio as the basis for allocation of constant costs. The 160 percent threshold represents an approximation of dollar ratio fully allocated cost at the revenue need level (FAC/RN/DR) plus the seven percent additive espoused in Flint Creek but rejected by the D.C. Circuit in San Antonio and the Tenth Circuit in Hiawatha. For example, FAC/RN/DR in Acco[8] of $6.46 is 147.8 percent of the embedded debt variable cost of $4.37. The seven percent additive applied to FAC/RN/DR would result in a rate at 158 percent of variable cost, very close to the Staggers Act jurisdictional threshold of 160 percent. Thus, the Staggers Act represents a legislative enactment of the judicially rejected seven percent solution.

Ton/ton-mile allocation of constant cost would subvert the Staggers Act. The entire regulatory scheme of the Staggers Act, providing for a phased increase of the jurisdictional threshold from 160 percent (first year), to 165 percent (second year) 170 percent (third year), 175 percent (fourth year), and a cost recovery percentage ranging from 170 to 180 percent thereafter would, in one fell swoop, be obliterated by the abrupt, arbitrary switch to the T&TM which immediately raises fully allocated cost in most cases above the 180 percent level intended by Congress only after five years. The legislative intent, manifest on the face of the statute, is reinforced by the Congressional Record of statements in the House of Representatives on the date of passage, September 9, 1980:

What we have attempted to do in this amendment is give the railroads the flexibility to price transportation services according to the marketplace, up to a certain threshold level. Over that threshold level, the ICC retains jurisdiction over rates. The amendment *gradually lifts that threshold level over a period of 4 years,* but the threshold never rises above 180 percent of variable cost. Similarly, we have provided a zone of freedom for railroads to raise rates without the fear of having such increases suspended or investigated unless the rate is 20 percentage points above the threshold. I emphasize that these are indeed *gradual, orderly forms* of pricing flexibility *that will not bring chaos to rail shippers.* [Italic added.] (Chairman Staggers, p. 8548).

Your proposal assures that H.R. 7235 will balance the competing demands for legislation to modernize rail regulatory policy. It assures competitive pricing wherever possible, and provides necessary protection for captive shippers. It phases in rate flexibility to avoid harshly imposing the burden of reforms, and responds to concerns raised about the level of the "cost recovery percentage." (September 4, 1980 letter from Esther Peterson, Special Assistant to the President for Consumer Affairs to Chairman Harley O. Staggers, Committee on Interstate and Foreign Commerce, House of Representatives, Washington, D.C., p. 8549).

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[7] Comments of Nevada Power Company in Ex Parte No. 347 (Sub No. 1), Coal Rate Guidelines—Nationwide. These costs were allocated by the T&TM method as applied by the I.C.C. in Docket No. 37409, Aggregate Volume Rate on Coal, Acco, Utah, to Moapa, Nevada, which allocated to coal constant costs wholly unrelated to the movement of coal.

[8] Docket No. 37409, *Aggregate Volume Rate on Coal, Acco, Utah to Moapa, Nevada.*

As a direct result of this legislative process, it has become possible to achieve a just solution. I earnestly hope that this amendment is adopted. It will provide guidance for the Interstate Commerce Commission from this Congress. *It will assure that the Interstate Commerce Commission does not proceed headlong into deregulation without guidelines* and without a bill from the Congress. If this measure were allowed to die, the circumstances that face captive shippers across our Nation would be in much more dire circumstances. This compromise amendment starts at the previously adopted Eckart-Rahall threshold level of a *160 percent* revenue variable cost percentage *above which review would be triggered by the ICC.* This revenue variable cost percentage, of 160 percent compares with the original 200-percent threshold level that previously existed in the original bill. The 160-percent level for 1981 is followed by 170 percent for 1982, 175 percent—or the cost recovery percentage, whichever is less—for the year ending September 1983.

After 1984 the threshold level that triggers access to the ICC and timely review of unreasonable rates for captive shippers, would be set at the cost recovery percentage, which in any event would not be less than 170 percent or more than 180 percent. (Emphasis added.) (Congressman Rahall of West Virginia, p. 8551.)

The compromise we have before us today provides for *deregulation in orderly stages* by raising the jurisdictional level of the ICC from a starting point of 160 percent with *annual increments of 5 percent* up to 180 percent of variable costs. The ICC would maintain jurisdiction over rates abvove the threshold. (Congressman Madigan of Illinois, p. 85766) (Emphasis added.)

How can ICC review be triggered at 160 percent, and how can there be deregulation in orderly stages if the ICC adopts a policy which automatically results in rates of more than 180 percent immediately?

From the foregoing it is clear that Congress knew that it was dealing with an Interstate Commerce Commission bent upon de facto deregulation and the Congress intended to restrain the Commission. The switch to T&TM allocation of constant costs would defeat the plain Congressional intent.

The Staggers Act is programmed to provide an astonishing rate of return. We do not concede the propriety of the legislative taking from captive shippers which inheres in such enormous returns. However, the enormous level of return which would be generated by the ultimate jurisdictional threshold serves to re-emphasize the legislative mandate, appartent on the face of the Act, and carefully explained by the Congressional sponsors, that rates be phased up gradually.

T&TM, URCS, and railroad proposed cost updating methodologies all would contravene Congressional intent.

The definition and use of the term "variable cost" in the statute is vague and indefinite, perhaps incurably so.

Section 202 of the Staggers Act provides that: variable costs shall be determined pursuant to section 10705a(m)(1) of this title, with adjustments specified by the Commission. 49 U.S.C. § 10709(d)(3).

The statute fails to set forth standards for "adjustments specified by the Commission." Moreover, section 10705a(m)(1) is equally vague and indefinite in that it provides that: variable costs . . . shall be determined . . . by . . . unadjusted costs calculated using the Commission's Rail Form A cost finding methodology *(or an alternative methodology adopted by the Commission in lieu thereof).* [Italic added.]

Nor does the statute set forth standards for "an alternate methodology adopted by the Commission in lieu thereof." Thus, apparently, "variable cost" may mean anything the Commission determines. But, wait. The Conference Report states:

The Conferees do not intend that the Commission alter the jurisdictional threshold by reducing the items which will be considered as part of the variable cost. (p. 91)

This clearly means that the ICC is not to increase its jurisdiction by reducing items included in variable cost. Thus the ICC may not redefine variable costs so as to exercise jurisdiction over lower rate levels.

May the ICC do the opposite, namely increase the items considered as a part of the variable cost thereby diminishing its jurisdiction and allowing rate levels to rise? The Report expressed no intention in this regard.

We shall soon see! The ICC proposes to adopt URC, in January, 1982, which will effectively increase the jurisdictional threshold by 20 points or more, unless adjusted to RFA comparability. But how will this be accomplished in view of the changed accounting system which makes calculation of current RFA costs extremely difficult, if not impossible, without access to carrier internal financial data? And how can the accuracy of URC costing be tested when it is to be based upon railroad inputs which the ICC proposes not to disclose, on an outmoded ICC computer which will not interface with other computers?

ıer the results must be the same as they would have been at the time of nent of the statute or the statute is incurably vague, indefinite, and one-sided. ıw will anyone be able to tell?

le it might be permissible in some other context to permit a regulatory to define variable cost in whatever manner that it was fit, it is incongruous dubious propriety to do so in the context of a statute which purports to the jurisdiction of an agency in terms of fixed percents of such variable costs. ıtutory jurisdictional threshold percents would be meaningless in the face of thority to redefine variable costs as it pleases.

goal of development of movement-specific costs which appears to be mandated requirement to: establish principles governing the determination of economi- ccurate . . . railroad costs directly and indirectly associated with particular ents of goods, including the variable costs associated with particular move- of goods or such other costs as the Board believes most accurately represent nomic costs of such movements. 49 U.S.C. § 11162(a) would seemingly result increased variability of costs, which would work at cross purposes with the ment that:

ı developing cost accounting principles under this section, the Board shall ıto account all the following considerations: (1) The specific regulatory pur- or which railroad costs are required. (2) The degree of accuracy of the cost ation which is needed to meet regulatory purposes. 49 U.S.C. § 11162.

t would seem to be a required and specific regulatory purpose to develop costs anner reflective of variability levels in effect at the time of enactment of the tage jurisdictional thresholds in the Staggers Act.

ection 203—Zone of Rate Flexibility.—This section contains the provision, others, that:

etermining whether a rate is reasonable, the Commission shall consider, other factors, evidence of the following: (i) the amount of traffic which is orted at revenues which do not contribute to going concern value and efforts to minimize such traffic; (ii) the amount of traffic which contributes only ıally to fixed costs and the extent to which, if any, rates on such traffic can nged to maximize the revenues from such traffic; and (iii) the carrier's mix of affic to determine whether one commodity is paying an unreasonable share of rier's overall revenues. . . . 49 U.S.C. § 10707a(e)(2)(C).

provision represents a codification of the differential pricing criteria set forth Flint Creek case.

railroads take the position that these statutory differential pricing criteria only to rate increases under the zone of rail rate flexibility, while shippers d that the quoted language, by its own terms, is not so restricted and that, in ent, it represents a restatement of those conditions which are a prerequisite d application of differential pricing.

ıe Acco decision, the Commission ignored both the statute and the Flint Creek ınd instead applied its own form of automatic differential pricing through ion of constant cost by the ton and ton-mile methodology. The Commission arched internally for a "quick and dirty interim method" of circumventing cision of the U.S. Court of Appeals for the District of Columbia Circuit in the ntonio case, pending approval of the ton and ton-mile methodology in an riate rule-making proceeding (which it feared might not meet the "concerns by railroad managers" in some unspecified fashion in advance of public nts)[9] but abandoned any attempt at an interim method and instead applied n and ton-mile methodology in the Acco case even though it had only been ed and not approved in the rulemaking proceeding Ex Parte No. 347 (Sub oal Rate Guidelines—Nationwide.

Commission's Acco decisions of February 6 and March 18 are a hybrid, since urported to determine costs on the ton and ton-mile method but used the methodology to do so. The railroads presented incomplete evidence and a Power no evidence of what costs might be on a ton/ton-mile basis and r the railroads nor Nevada Power addressed the rationale underlying T&TM all prior cases were based upon the dollar ratio method. No hint was given he Commission might decide to switch as a matter of policy to ton/ton-mile dology. The suggestion of ton/ton-mile in Ex Parte No. 347 (Sub. No. 1), Coal Guidelines—Nationwide, came 50 days after the final evidentiary filing in

I.C.C. internal working documents obtained through F.O.I.A. requests and included in nts of Nevada Power Company filed May 11, 1981 in Ex Parte No. 347 (Sub No. 1), Coal uidelines—Nationwide.

But the Commission's staff had been busy trying to overcome the disastrous (to the railroads) remand of the San Antonio case and the seeming end of the arbitrary 7 percent additive.

On June 20, 1980, only 11 days after the presses had dried on the D.C. Circuit's reversal of the I.C.C., its staff addressed the means for circumventing the Court in a memorandum entitled, "Proposed approach to issues raised in San Antonio." This memorandum illustrates what is wrong with Commission rate-making. It concludes with:

Second, we will need a quick-and-dirty interim method of dealing with pending cases without reliance on the 7 percent solution or the new 347 approach that will not yet be in place. Here I think we can proceed by plugging some numbers into the method outlined in the SWEPCO decision, that is, by using a crude and high estimate of the required additive reduced according to our reasoned policy judgment to something in the neighborhood of 7 percent or whatever it comes out to be. (Id. at 4.) (Emphasis added.)

Consider the implications. The staff seeks an "interim method," and would thereby pile a new set of mistakes upon an old while awaiting a third. And what is this "interim method?" Why just plug in "some numbers" and use a "crude and high estimate." Such is the art of rail ratemaking after 95 years. Then the "estimate" is reduced "according to our reasoned policy judgment." The quick-and-dirty interim method is a temporary substitute for the arbitrary 7 percent additive until the I.C.C. could approve the quick-and-dirty permanent method of the equally arbitrary T&TM in Ex Parte 347. If this approach is not a textbook illustration of the definition of arbitrary and capricious, then nothing is!

Indeed, the "quick-and-dirty interim method" has been the essence of I.C.C. rate-making. Short-sighted solutions. An endless succession of thumbs in the dike.

The same memorandum also stated: I recommend changing to the ton mile method. If we make this change, we should justify it by explicit appeal to differential pricing, arguing that heavy-loading commodities are, on the average, more likely to be captive to rail, and hence more likely to be demand-inelastic, than light-loading commodities. This will give a substantial element of built-in differential pricing, thus reducing or eliminating the necessity for a percent additive.

Note the reasoning process, which would seem a fair summation of the I.C.C.'s approach in Ex Parte No. 347. The I.C.C. is urged to make the change and "justify it by explicit appeal to differential pricing, . . .". Nowhere is it stated that as a result of extensive studies it can be concluded that there is a factual basis for the ton and ton-mile method. Nowhere does it state there is evidence submitted in a proceeding upon which the I.C.C. can rely for the suggested conclusion. In other words, the memorandum proposed that the I.C.C. move to ton-mile because it is a convenient substitute for the rejected 7 percent solution.

In summary, the I.C.C.'s rate-making process went like this: it had already decided within days of the reversal of the arbitrary 7 percent additive to adopt the equally arbitrary T&TM solution and needed an interim solution until it could formally propose and approve the T&TM solution in Ex Parte No. 347. In issuing its Notice of Proposed Guidelines [10] November 18, 1980, the I.C.C. noted the passage of the Staggers Act, but failed to recognize, in proposing the T&TM (ton/ton-mile) method of allocating constant costs, that the Staggers Act had, through the establishment of jurisdictional threshold percentages, approved the DR (dollar ratio) method of allocating constant costs and required that any rates above the threshold percentages be fully justified in terms of the statutory differential pricing criteria. Then, in Acco, where the parties did not address the merits of T&TM because the record was closed prior to the T&TM proposal in Ex Parte No. 347, the I.C.C. adopted T&TM citing its proposal in Ex Parte No. 347. Thus having approved T&TM in Acco, it proceeded to cite the approval in Acco as grounds for applying T&TM in other rate-making cases, as well as rulemaking decisions, even though evidence and public comments had not yet been filed in Ex Parte No. 347.

Thus, while the quoted statutory provision appears to require consideration of those three elements with respect to any rate above the jurisdictional threshold, the Commission has negated those provisions to the extent that ton and ton-mile allocation of constant cost applies a new rate floor for captive coal traffic far in excess of the jurisdictional threshold.

5. *Section 205—Rate Regulation Proceedings; Adequate Revenue.*—Aside from the Commission's strange interpretation of the "product competition" provisions of this

[10] Note that the I.C.C. proposes "guidelines" or "policy" instead of "rules" whenever it seeks to avoid the strictures of the Administrative Procedure Act pertaining to rulemaking.

., it has further interpreted this Section so as to require redefinition of its
rds of railroad revenue adequacy.
x Parte No. 393, Standards for Railroad Revenue Adequacy, it has proceeded
ndon all of its long-standing indicators by which revenue adequacy is tested
is substituted in lieu thereof as the sole determinant the current cost of
, thereby enabling the Commission to find that no carriers, with the excep-
three small and inconsequential ones, enjoy revenue adequacy. By this
ion, the Commission has declared inadequate the revenues of completely
y carriers, thereby enabling them to lay claim to numerous increased-pricing
ges accorded by the statute only to revenue inadequate carriers. The legisla-
story fails to disclose any contemplation by Congress of this gross perversion
I.C.C. of the concept of revenue adequacy. Its action ignores all of the other
lly accepted standards for determination of corporate financial health, includ-
e of return on equity, throw-off to debt ratio, rate of return on total capital-
, and fixed and contingent charge coverage.[11]

ction 206—Inflation-Based Rate Increases.—Because of the methodology in-
the increases authorized by this Section tend to impact disproportionately
flate further the return upon captive coal traffic. This impacts adversely upon
al energy and inflation interests.

ction 208—Contracts.—In Ex Parte No. 387, Railroad Transportation Con-
the Commission has ignored the statutory requirement that "the essential
of the contract are available to the general public," treating most of the
al terms as confidential, thereby encouraging favoritism, discrimination and
wth of monopoly power, both among carriers and shippers.

rate contracts are not available on reasonable terms to captive shippers since
is neither incentive nor requirement that such contracts be offered. In prac-
e statutory schemework, implemented by the Commission, is a disincentive to
e of contract rates for captive traffic. Since the jurisdictional thresholds and
mmission's ratemaking proposals set rate floors and not rate ceilings, carriers
willing to subject themselves to contractual restraints upon their rate levels.
he extent that the Commission had made limited disclosure of the terms of
te contracts, such disclosure fails to indicate the extent to which such con-
may have been competitively inspired.

pt for one, these contracts involve eastern railroads which usually have
costs than the western railroads. The summaries generally fail to provide
nt information concerning rates and operating conditions from which the
ableness of the contract rates can be ascertained. There are a number of
les of contracts tying in with rail-owned loading, unloading, or port berthing
es with the contracted volume at such a level so as to preclude or limit the
the tied-in facility by other shippers and carriers.[12]

ad of leading to competitive pricing, secret rail contract ratemaking may
rate into a farce of predatory pricing, destructive competition, discriminatory
g and rebates, and evasion of the anti-trust laws at the expense of captive coal
rs, the national energy policy and spiraling inflation.

he extent that rail rate contracts are offered to shippers of coal, they are
lly offered by the railroads on a take-it or leave-it basis. Rail rate contracts
ely do not provide any solution for captive traffic.

ection 216—Efficient Marketing.—The Commission has clearly abused the
ry intent through the combined effect of its actions in Docket No. 37517,
tion of the Notice Period of Filing Railroad Tariffs, and Docket Ex Parte No.
rotests Against Tariffs and Rules of Practice Governing Procedures in Certain
sion Matters.[13]

e name of efficient marketing, Section 216 has reduced the time for effective-
f rail rate actions from 30 days to 20 days for increased or new rates and 10
or reduced rates. The Commission has modified its rules that formerly pro-
that protests should be filed not less than 5 days before the effective date of
ations made on less than 30 days' notice, and provided that protests against
hanges filed on 20 days' notice shall reach the Commission at least 10 days
the proposed effective date. This action shortens the time for filing a protest
15 to 10 days, making it virtually impossible in many cases for shippers to
e and file an adequate protest.[14] Moreover, the Commission has construed

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ening Statement of Facts and Argument of Nevada Power Company on Reopening filed
ber 9, 1981 in I.C.C. Docket No. 37038, Bituminous Coal, Hiawatha, Utah to Moapa,
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e summaries of coal contracts disseminated by the I.C.C.'s Contract Advisory Service.
e comments in Docket No. 37517 and Petition to Reopen and Consolidate in Ex Parte 398,
nuary 26, 1981 by Nevada Power Company.
hen rates were filed on 30 days' notice, shippers had 18 days in which to protest.

out of existence the term "new rate" requiring 20 days' notice under the Staggers Act and issued rules which will enable carriers in the future to claim that most rate publications are decreases entitled to only 10 days' advanced notice, rather than 20. The Commission has noted that "there is almost always some rate published and in effect which would be applicable to a given shipment" in view of the "more than 100 years the railroads have operated" and that "an extensive rate structure has evolved." It then cites a carrier publishing a lower commodity rate when a class rate is in existence as an instance of a reduced rate rather than a "new" rate.

Thus, the I.C.C. has defined out of existence the statutory term "new rate" and thereby apparently affords carriers the right to publish on 10 days' notice, as a rate reduction, an exorbitant annual volume coal unit-train rate, where there was previously on file nothing more than a single car class rate. This end result would be a gross perversion of a the statutory intent and a radical departure from past Commission decisions. The end result of this change would be that it would possibly allow carriers in the future to file on 10 days' notice, rather than 20, rates such as those investigated in Docket No. 37038 (Hiawatha) and in Docket No. 37409 (Acco).[15] There would be, apparently, only 5 days to protest, instead of the previous 18 days.

The combined effect of the Commission's actions is to stifle the ability of shippers to assert their rights through the filing protests.

9. *Section 220—Long and Short Haul Transportation.*—Although Congress carefully considered the long and short haul clause and determined to repeal only a limited portion thereof, the Commission would invoke its general exemption authority to nullify not only the statute but also long established case law by means of the rule-making proposal in Ex Parte No. 346 (Sub No. 3), Rail General Exemption Authority: Long and Short Haul Transportation.[16] The I.C.C. has exceeded its general exemption authority in proposing to nullify, in major part, the long and short-haul and aggregate of intermediate clauses and to reverse, by implication, a decision of the Supreme Court, which held: Apart from statutory enactment it is prima facie unreasonable to charge more for a shorter than for a longer haul. To charge more for a through haul than the aggregate of the intermdiate rates is likewise prima facie unreasonable. *Patterson v. Louisville & N.R. Co.,* 269 U.S. 1, 70 L.Ed. 131, 137 (1925).

10. *Section 221—Railroad Entry.*—The Commission has done little, if anything, to encourage new railroad entry in monopoly situations.

11. *Section 229—Savings Provisions.*—Although the Commission rushed out a press release at the time of the signing of the Staggers Act in order to proclaim various other effects, it did nothing to publicize the fact that § 229 would operate to exterminate shipper rights to complain about existing rates after the expiration of 180 days. Notwithstanding, more than 800 complaints were filed by shippers under § 229. The processing of these complaints poses an enormous burden for the Commission, industry, and public alike. The full ramification of these proceedings has just begun to be explored.[17] If the Commission is to afford due process to the parties involved in these proceedings, it must receive increased staff support. While the Commission is hoping, and groping, for easy or simplified solutions it should be apparent from the complexity of rail rate litigation as reflected in the Staggers Rail Act and the numerous rule-making proceedings pending before the Commission and the courts that an increase in the number of administrative law judges and attorney and cost staff support will be required for efficient and just disposition of these proceedings. This difficult problem must be addressed promptly and forthrightly notwithstanding the overall climate of budgetary constraints. Failure to do so and substitution of quick-fixes and short-sighted solutions will almost inevitably result in court reversals protracting the ultimate disposition of these proceedings for many more years to come.

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[15] The carriers contended in Acco that the rate proposal was a reduction over which the I.C.C. could not exercise maximum rate jurisdiction. They also claimed that, as a reduction, the rate was subject only to minimum, not maximum, rate standards. They lost on this issue in Acco. The combined effect of Dockets No. 37517 and Ex Parte No. 398 apparently might also result in the opposite decision on this issue in future cases, thereby eliminating important substantive shipper rights. This combined effect has escaped public recognition. It may even have escaped recognition by the I.C.C. and been unintended in proposing these rules.

[16] See Comments of Nevada Power Company filed January 17, 1980 and February 23, 1981.

[17] See, for example, Docket No. 37622, Petition for Declaratory Order—Existing Railroad Rates, and the court appeal thereof; Notices of Docket Management Conference in § 229 Cases; and the Motion to Dismiss filed by the railroads, and Petition for a Declaratory Order filed by numerous shippers in Ex Parte No. 411.

Whether it receives additional staffing or not, it appears inevitable that the I.C.C. will be unable to complete the numerous § 229 proceedings within the 3 year period required under 49 U.S.C. § 11701 and that it will find it necessary to request legislation to extend the time within which it may process these cases. Perhaps another solution would be the outright repeal of § 229. Although labelled "savings provisions" that section saves nothing, but instead extinguishes the rights of shippers to complain about existing rates after a 180-day period. If the section is repealed, with the provision that existing complaints may be dismissed without prejudice, and shippers would be allowed to file complaints in the future, as they have always been able to do in the past, then the need for consideration of many of these complaints would undoubtedly disappear for the present and might never reappear.

III. TWO BASIC PROCEDURAL PROBLEMS

The Commission has adopted two basic procedural practices which frustrate shippers' rights:

1. It has proposed major changes in rate-making criteria in notices of proposed rule-making and then proceeded to implement those changes, resulting in higher rate levels, in individual rate-making cases prior not only to ultimate resolution, but also prior even to receiving comments in the rule-making proceedings. For example, the proposals in Ex Parte Nos. 347 (Sub No. 1) and 393 were implemented in the rate decision in the Acco case, thereby substantially inflating the maximum rate above that which would have been approved under existing standards. The interlocking and bootstrapping of cases unduly burdens shippers by requiring them to cover all bases in order to protect vital interests. Moreover, the implementation of changes in rate-making proceedings, which are being concurrently proposed but have not yet been approved in rule-making proceedings, is a radical departure from sound regulatory principles.
2. It has adopted a practice of issuance of notices of proposed guidelines or proposed policy rather than proposed rule-making. Through this practice, it sets forth fuzzy statements, circumventing Staggers Act and Administrative Procedure Act requirements for standards and procedures, thereby enabling the Commission to do as it pleases without any cognizable standards by which its actions can be judged—for example, Ex Parte No. 320 (Sub No. 2), Market Dominance Determinations and Consideration of Product Competition, and Ex Parte No. 347 (Sub No. 1), Coal Rate Guidelines-Nationwide.

These practices should be terminated.

CONCLUSIONS

When the Staggers Rail Act of 1980 was passed it was hailed by the Administration as completing its goal of deregulating transportation by air, truck and rail.

However, the Staggers Act does not really deregulate. It merely allows the carriers to increase substantially their prices on captive traffic and to lower substantially their prices on competitive traffic which is subject to intermodal competition. The Staggers Act, as implemented by the I.C.C., has so complicated and intensified regulation as to defy the regulated, the public, and indeed the Commission, to keep abreast of developments.

The complexities of the statute have been exacerbated by a Commission that never paused long enough to appraise the effects of the Staggers Act, if literally applied, and either ignored or distorted the plain meaning of numerous provisions of the statute so as to plunge onward in its course of de facto abandonment of pricing restraints on captive and competitive traffic. The rulemaking and ratemaking activities of the Commission were carefully orchestrated by the A.A.R. through the I.C.C.'s Office of Policy and Analysis. Review of the Commission's Notices of Proposed Rulemaking and ratemaking activities in light of the policy memoranda generated by the O.P.A. indicates that the purpose was to authorize "more," without defining how much "more" is "more," with respect to maximum rates.

As a consequence of the program to rationalize goals rather than to apply the facts, law, and sound economic principles, the I.C.C.'s ratemaking and rulemaking processes have been left in a shambles. Because of the bias and predisposition in favor of the railroad displayed in the various notices of proposed rule-making, shippers have come to expect that the ultimate rule-making decisions will in every instance require court review in order to accord them the protections intended in the statute.

Unless the Commission voluntarily re-examines the rationales and effects of the numerous interrelated rule-making proceedings, it will be many years, if ever,

before a rationalized regulatory policy is developed as a consequence of piecemeal court remand, reopening, and reconsideration.

Congress and the I.C.C. must both recognize the need for continued protection of the public interest against the potential abuses of rail monopoly power. Both must also recognize that just administration of this complex statute will require increased resources, rather than short-cut solutions.

It is recommended that the subcommittee tentatively conclude:

1. Certain provisions of the Staggers Act may be inconsistent with our national transportation and energy interests. The enormous rate of return for transportation of captive coal at jurisdictional threshold levels, and availability of differential pricing to establish coal transportation rates at even higher levels to make up revenue shortfalls due to depressed rate levels on intermodally competitive traffic may impact adversely on both energy interests and the general economy. The economic effects of the large cross-subsidy implicit in the Staggers Act, even at jurisdictional threshold levels, should be studied.

2. The basing of Jurisdiction upon fixed cost ratios may result in increasing difficulties. The Cannon bill S. 1946 was much sounder conceptually in providing for a jurisdictional level equal to the average ratio of revenue to variable cost for all transportation. This standard would survive changes in costing methodology. It also would avoid the enormous automatic tax upon coal and other captive traffic, and cross-subsidy of non-captive traffic, implicit in fixed percentage jurisdictional thresholds.

3. The statute itself is exceptionally complex and has resulted in extensive litigation. Only through proper understanding and implementation of the statute may the goal of less litigation be achieved.

4. The I.C.C. has ignored the intent of the Staggers Act and has continued to plunge ahead on its course of de facto deregulation by establishing new rate floors substantially in excess of the jurisdictional threshold, thereby rendering the statutory cost threshold meaningless.

5. The I.C.C. has perceived a mandate to raise rail rates and has proceeded to rationalize means to achieve that mandate, rather than develop an economically sound regulatory theory. It has ignored the case law and statutory criteria prerequisite to differential pricing and has proceeded to impose arbitrary differential pricing upon captive coal traffic through ton and ton-mile allocation of constant cost in disregard of statutory intent, and national energy and transportation interests.

6. Because of the ability of monopoly railroads to extract huge price mark-ups from captive shippers in the absence of regulation, the I.C.C. and railroads have viewed the cost percentage jurisdictional thresholds as a rate floor rather than a rate ceiling. The ICC has therefore continued to cast about for means to rationalize higher rates above full cost. Prior to the Staggers Act the device was the 7 percent additive. Now it is ton and ton-mile constant cost allocation. This inability to draw the line encourages the railroads to continue to test the waters with one outrageous proposal after the next—the latest being Ramsey pricing, whereby rates would be set in inverse proportion to the elasticity of demand—which simply means the sky is the limit for monopoly traffic. Thus, each new concession to rail demands by an I.C.C. motivated to give enough, without knowing how much more is enough, will only be met with more demands by railroads professing not to be satisfied. The I.C.C. must draw the line.

7. The regulatory solution is to follow the legislative intent and enforce the statute: treat the jurisdictional threshold as a rate ceiling for captive traffic except in extraordinary circumstances where the carrier is able to satisfy fully the 3-point differential pricing criteria of Section 203 of the Staggers Act, the Long-Cannon amendment, 49 U.S.C. 10707a (e)(2)(C). Thus there will be less regulation, instead of more, because the railroads will be forced to discipline themselves in their lowside pricing.

8. Continuing legislative oversight is required.

It is also respectfully recommended that this Subcommittee initiate a staff study of

(1) the I.C.C. implementation of the statute, and

(2) the effects of the Staggers Act and its soundness in terms of economic and regulatory principles and our national energy and inflation policies.

I thank the Committee for this opportunity to present my views and will be pleased to provide additional details, as well as copies of the various documents referenced herein.

Senator DANFORTH. Thank you very much, Mr. Lawson. I am sorry to say there is another vote. We will go on to Mr. Morgan in about 10 minutes.

[Recess.]

Senator DANFORTH. Mr. Morgan?

Mr. MORGAN. Mr. Chairman, my name is Walter E. Morgan, chairman of the legislative committee of the National Industrial Traffic League. With me today is John F. Donelan, league general counsel. The league supports the objectives of the Staggers Rail Act of 1980. Although the measure does not include all the reforms we advocated, we endorse it as the best means of achieving our overall goal—eliminating unnecessary Federal regulation. Since enactment, we have been actively involved in the law's implementation, and have been a party to all rulemakings involving broad-based issues.

While it is too soon to make a definitive statement about the ultimate success or failure of the Staggers Act, we believe that there have been some early warning signals that could act to undermine the reform measures carefully constructed and crucial balance. The strongest of these affect the standards used to determine whether a shipper has the right to seek Federal redress when it believes itself to be the victim of an abuse of market power—market dominance; the standards used to determine whether the rail industry is making sufficient capital to attract investment, revenue adequacy; and the standards used to compensate carriers for their inflationary costs. In addition to these, the league believes that the subcommittee should be aware of other potential disruptions affecting contracting, loss and damage liability, antitrust immunity for collective ratemaking, as well as the current level of merger activity in the rail industry.

In closing, the league believes that the Staggers Act will realize its goals of providing a balanced reform of the Federal regulations governing our Nation's railroads, and of providing the necessary impetus to insure their revitalization.

However, if the early warning signals we have outlined aren't heeded, and corrective action taken, or, if the law's careful and complex balance of the needs of all parties is upset, or if these warning signals are ignored, the Staggers Act will prove to be no more successful in achieving our commonly shared objectives than its predecessor—the 4R Act of 1976. We offer the subcommittee our continuing support to realize the balanced reform of these laws, and to provide the railroads with the tools necessary to insure their revitalization. We look forward to being able to return next year to further report in greater detail on the shippers' experience under this legislation.

Thank you for this opportunity to comment.

[The statement follows.]

STATEMENT OF WALTER E. MORGAN ON BEHALF OF THE NATIONAL INDUSTRIAL TRAFFIC LEAGUE

Mr. Chairman, members of the subcommittee, my name is Walter E. Morgan. I am chairman of the Legislative Committee of the National Industrial Traffic League. Accompaning me today is John F. Donelan, League Counsel.

The National Industrial Traffic League is a voluntary organization of 1,800 shippers, shippers' associations, chambers of commerce, boards of trade, and other

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entities concernec with rates, traffic, and transportation services of all modes. It is the only nationwide organization which represents all types of shippers using all modes of transportation to move all types of commodities. Our members, directly or indirectly, are responsible for the routing of about 80 percent of our country's commercial freight.

The League's primary concern is to assure that our national transportation system is sound, efficient, well-managed, and privately owned and operated, and that it meets the needs of our nation as well as those of shippers and receivers of commercial freight. To arrive at the policies and positions reflecting our broad range of interests, our members, at least annually, consider, debate, and vote on pertinent transportation issues. Throughout our more than 70-year history, the league frequently has been the spokesman for business and industry on transportation matters.

The League supported the objectives of the Staggers Rail Act of 1980. Although the measure did not include all the reforms advocated by the League, we endorsed the compromise legislation as the best means of achieving our overall goal of eliminating unnecessary federal regulation. Since enactment, we have been actively involved in the law's implementation and have been a party to all rulemakings involving broad-based issues. Overall, we commented in about half of the Interstate Commerce Commission rulemakings seeking public comment.

For your information, we have attached to this testimony a synopsis of the League's positions in these proceedings. We would be happy to supply the subcommittee with the full text of any filing. The positions advocated in these proceedings are based upon current League policy and upon recommendations from the general membership. In espousing these positions, the League recognizes each member's right to independent action.

From a shipper's standpoint, the standards used for judging the effectiveness of the Staggers Rail Act are different from those used to evaluate last year's Motor Carrier Act. Unlike the Motor Carrier Act, which eased regulatory burdens imposed on competitive and captive traffic, the Staggers Act dealt essentially with rates on captive traffic. The railroads were freed from federal rate controls over competitive traffic when the 95th Congress passed the 4–R Act of 1976.

Thus, from our perspective, the issues in the rail reform measure were much more complex than those facing Congress in the trucking reform law. Instead of reforming laws originally designed to foster an infant industry that has since matured into an integral part of our national transportation system, we perceived the 96th Congress, in the Staggers Act, to be grappling with the problems of how does one define captive traffic and what types of pricing flexibility should be granted for this type of freight.

We view the role of the 97th Congress in this area as ensuring that the balancing of the interests of all parties—shippers, carriers, and in public—is preserved both during and after the law's four-year phase-in period, and that no one party is placed at a competitive disadvantage as the federal agencies and the courts implement and oversee this complex measure.

While it is too soon to make definitive statements about the ultimate success or failure of the Staggers Act, the League believes that there have been some early warning signals that could act to undermine this carefully constructed and crucial balance. The strongest of these signals emerge in the following areas: (1) the standards used to determine whether a shipper has the right to seek federal redress when it believes itself to be the victim of an abuse of market power; (2) the standards used to determine whether the rail industry is making sufficient capital to attract investment; and,, (3) the standards used to compensate carriers for their inflationary costs.

With respect to the issue of the right to federal redress—market dominance, shippers are deeply disturbed about the injection of geographic and product competition as primary elements in this process, and about the shifting to shippers of the evidentiary burden of going forward when the rail industry raises the issues. These considerations will unreasonably complicate the evidentiary question of whether a carrier indeed has market control in a specific situation and whether the rates at issue are unreasonably high.

The practical result of applying these concepts here is that, unless a shipper's customers are unable to buy the goods at issue from another source, the shipper has no right to seek review of its carriers' rates. Allowing these considerations to become part of determining whether a shipper has the right to seek review of a rate it believes is unreasonably high will place shippers and their customers at a severe disadvantage.

We would strongly urge the subcommittee to reaffirm that shippers which do not have the advantage of effective competition do have the right to seek federal review

of what they believe to be a carrier's abuse of its market power. We seek Congressional clarification to ensure that the balance between the railroads' need for greater rate freedom and the shippers' need for redress against suspected abuses of market power is not substantially impaired and ultimately destroyed.

With respect to whether the rail industry is making sufficient capital to attract investment—revenue adequacy, the League has serious reservations about the standards currently used by the Commission to determine cost of capital and about the rate base to which this cost should be applied. In its most recent decision, the Commission used methodologies that will artificially increase the amounts of capital needed by the railroads and, in turn, unnecessarily increase the costs of transporting goods—a cost that will ultimately be absorbed by the public.

Under these standards, the ICC found that only three Class I carriers in the country were making a return sufficient to meet their capital needs. They were the Bessemer & Lake Erie, the Elgin, Joliet & Eastern, and the Fort Worth & Denver. We find this disturbing since the industry itself reports that 1980 was a banner year—resulting in the highest revenues since 1945—and since recent press reports indicate that the industry next year will receive what could amount to a $1 billion tax break as a result of provisions contained in the recent tax legislation.

This ruling has a profound effect on shippers because the Staggers Act inhibits regulatory challenges to rate increases and expands the zone of rate freedom for carriers whose revenues that fall below this agency standard. We would urge the subcommittee to carefully monitor the Commission's actions in this area to ensure that these revenue adequacy standards are set at realistic levels which allow the rail industry to attract capital, and which do not arbitrarily abrogate a shipper's right to federal regulatory redress.

With respect to compensating carriers for their inflationary costs, the League is concerned that the agency's current methodology for computing these costs does not accurately reflect actual market conditions since it fails to make any adjustments for offsetting productivity gains, and fails to provide shippers with any meaningful input into the computation process.

Under present procedures, the Association of American Railroads presents its data to the agency; the agency then reviews and makes a final judgment on it without ever receiving comment or input from the shipping community as to its accuracy. While we recognize and support that carriers must be able to offset the impact of inflation on their operating costs, we believe that the methodology and standards used for this compensation must accurately reflect market conditions and be structured in such a way to endure that they retain their original purpose—to offset inflation, not increase profit margins.

We would urge the subcommittee to carefully monitor this ratemaking device to ensure that it retains its original purpose and does not become a means of windfall profits to the carriers.

In addition to these early warning signals, the League believes that the subcommittee should be aware of other potential disruptions to the Staggers Act's careful balance.

In the contract area, there are three signals of which the subcommittee should be aware. The first involves the Commission's rules governing these useful rate and service devices. Since the ICC has withdrawn its interim and has yet to issue its final rules, shippers are becoming uncertain about entering into these agreements without first having clear-cut guidelines. The longer that these rules are held in abeyance, the greater the uncertainty. The League would urge the subcommittee to review the agency's actions in this area and to take actions that will help to eliminate the current misapprehension and confusion.

The second involves the relationship of contracts with the regulations governing tariff filings. Since the new law exempts contracts from these requirements, there is a growing sentiment that unless each contract specifies all of these regulations as part of its terms, shippers are without guidance or protection. The League would recommend that the subcommittee consider a minor change to the law to eliminate this uncertainty. The change would clarify that contracts included these regulations unless otherwise specified in the terms of a contract.

The third involves the status of a contract if minor changes are made after receipt of Commission approval. Since there is no mechanism for Commission action on a contract after the agency's grant of initial approval, shippers fear that any minor changes made in the terms of the contract could result in a revocation of the contract's exemption from agency review. The League would urge the subcommittee to clarify that such minor changes are permissible.

In the liability and claims area, the League agrees with the Commission that the following changes should be made: (1) venue and federal court jurisdictional thresholds be repealed; (2) successful claimants be awarded attorney fees. In addition, we

would urge the subcommittee to consider: (1) eliminating the deductibles established by the Staggers Act; (2) allowing review of the reasonableness of the difference between full and released value rates; and, (3) reviewing the procedures for tariff and rule filings to prevent carrier abuses in limiting liability, especially in the intermodal area.

Another point we would like to bring to the subcommittee's attention is the current merger activity in the rail industry. While we support soundly conceived mergers that tend to strengthen the transportation industry, we are concerned that the dimunition in the number of carriers could result in the ever-increasing elimination of effective competition. It is not improbable that, within the next decade or so, today's 35 Class I railroads could be reduced to between four and six. It is important that as these mergers reduce the number of competitors, Congress continue its oversight efforts in light of these changed circumstances.

A final point we would like to make is the need for clarification on shippers' right to participate in the carriers' collective ratemaking process. The current uncertainty has chilled shipper participation in the ratemaking process and sharply curtailed their appearances before the rate bureaus. We would urge the subcommittee to reaffirm shippers' long recognized and utilized right to appear, either collectively or individually, before rail rate bureaus.

This uncertainty also has inhibited the law's intent to allow shippers and carriers to solve the private car compensation problem. Although the Staggers Act allowed shippers, after receiving Commission approval, to consult among themselves as a preparatory step to entering into compensation negotiations with the carriers, the ICC has failed to act on any of the shipper petitions seeking this antitrust authority.

In closing, the League believes that the Staggers Act will realize its goals of providing a balanced reform of the federal regulations governing our nation's railroads and of providing the necessary impetus to ensure their revitalization, if the early warning signals we have outlined are heeded and corrected. If the law's careful and complex balance of the needs of all parties is upset or if these warning signals are ignored, the Staggers Act will prove no more successful in achieving these commonly shared objectives than its predecessor—the 4-R Act of 1976.

We offer our continuing support to the subcommittee's efforts to realize a balanced reform of these laws and to provide the railroads with the tools necessary to ensure their revitalization. We look forward to being able to return next year to further report on shippers' experience under this reform law and thank you for this opportunity to present our views. We now would be glad to answer any questions you may have.

ATTACHMENT SUMMARY

Ex Parte No. 230 (Sub-No. 5), Improvement of TOFC/COFC Regulation

The League essentially supported the Commission's actions. It also urged the agency to clarify that the exemption also removed the carriers' antitrust immunity for collectively setting per-diem rates and charges on trailers and containers.

Ex Parte No. 290 (Sub-No. 2), Railroad Cost Recovery Procedures

The League challenged the Commission's decision on the following points: (1) there is a need for the shipping public to have the right to inspect and examine, in advance, the methodology and underlying working papers used to determine the cost index; (2) there is a need for the shipping public to have the right to submit their analyses, comments, and suggestions prior to the agency making its final determination of the appropriate cost index; (3) the Commission, not the rail industry, should have total responsibility for the index's methodology and implementation; and (4) these rate increases should be filed on 20 days' notice.

Ex Parte No. 32030 (Sub-No. 2), Rail Market Dominance and Consideration of Product Competition

In the first phase of this proceeding, the League challenged the Commission's decision on the following points: (1) geographic and product competition have no useful role in determining the reasonableness of a given rate; and, (2) efforts by the rail industry to reverse or delay this ruling should be promptly denied, and its contention that the effective date of this decision be delayed until after a ruling is made in Ex Parte No. 347 (Sub-No. 1) is unwarranted. In the second phase of this proceeding, the League objected to: (1) the termination of the rebuttable presumptions of market dominance; (2) its disregard of the statutory definition of market dominance; and, (3) the distorted and exaggerated role accorded product and source competition in determining the market dominance issue.

Ex Parte No. 387, Railroad Transportation Contracts

The League essentially supported the Commission's interim decision. It urged the agency to clarify that: (1) the contract tariffs should be made available to the public on the same basis as other rail tariffs; (2) these tariffs and contract summaries should be genuinely informative so that shippers may determine the compliance of a given contract; (3) access to the actual contract should be allowed upon a meaningful demonstration that such access is necessary to enforce the rights of the parties; and, (4) final rules appropriately reflect the procedures outlined in section 208 of the Staggers Rail Act.

Ex Parte No. 389, Procedures for Requesting Rail Variable Cost and Revenue Determinations for Joint Rates Subject to Surcharges or Cancellations

The League generally supported the Commission's decision. It urged the agency to clarify that: (1) requests for variable cost or revenue data on proposed surcharges or route cancellations are to be made via registered or certified mail, returned receipt requestled; (2) agency responses to those requests will be made in writing; and, (3) the ICC will assume total control of this process and not delegate it to outsiders.

Ex Parte No. 393, Standards for Railroad Revenue Adequacy

The League challenged the Commission's decision on the following points: (1) the agency proposal is contrary to the Staggers Rail Act and incompatible with the Federal Administrative Procedures Act; and (2) the ICC should concentrate its efforts on refining funds flow methodology, developing standards for economical and efficient management, and scrutinizing carriers' original cost net investment rate base.

Ex Parte No. 399, Cost Recovery Percentage

The League essentially supported the Commission's decision. It urged the agency to clarify that: (1) the shipping public should be granted maximum access to and input during all phases of the CRP's determination—both in the formulation of the overall methodology for calculation and in the calculations of annual individual figures; (2) shippers and carriers have full opportunity to comment on the underlying data for each year's computations and on any changes to the overall methodology; and, (3) the finally approved methodology for determining the CRP should be published in the form of official agency rules.

Ex Parte No. 403, Cargo Liability Study: Report to Congress

The League supported the Commission's decision. It supported retaining current liability standards, and found vital to ensuring the fair treatment of the shipping public the retention of full-value, strict-liability rates.

Senator DANFORTH. Thank you, Mr. Morgan.

Mr. Griffin?

Mr. GRIFFIN. Mr. Chairman, members of the subcommittee, my name is Donald G. Griffin, vice president, PPG Industries. With me today is Gloria Sodaro, staff counsel for the Chemical Manufacturers Association. CMA appreciates the opportunity to appear today to present its views on the first year under the Staggers Rail Act of 1980.

CMA supported enactment of the rail regulatory reform because of the importance of a strong, safe rail system for our industry. We well remember that the primary object of last year's legislation was to enable the railroads to improve their financial posture. We also remember the objective of providing continued protection to the captive shippers. We supported the act because we believed at that time there was a reasonable balance between the carriers' financial needs and the shippers' interests.

We are especially concerned about captivity, because we have several factors that make us uniquely captive. We have over 1,500 plants which are designed primarily to use the U.S. rail system, most of them located on single lines. The nature of our products requires that we ship by rail. Most significantly, we are running over 100,000 cars, with a replacement value up to $5 billion, on the

U.S. rail system. That is captivity. We are not getting ready to move off on another mode in the morning.

What is the chemical industry's reaction to the first year under the Staggers Act? Frankly, we have been greatly disappointed with the failure of the ICC to develop regulations to implement provisions in a manner that struck a balance that we thought was in the act. In my written testimony, we addressed several ICC actions which we believe are contrary to the compromise in the act. We are going to address two or three.

First and foremost are the market dominance guidelines. The ICC's substitution of evidentiary guidelines for the presumptive test of market dominance has made it much, much more difficult than Congress ever intended for shippers to procure ICC review of the rail rates, even those above 190 percent of revenues over variable costs—where we thought we needed the protection.

We are dismayed by the ICC's inclusion of product and geographic competition in market dominance determination. This is not only contrary to the letter and spirit of the law, but is a critical jurisdictional step into a much too complicated and burdensome process that disrupts the careful balance that this committee worked so hard to achieve last year. You should see some of the questionnaires that we are getting on market dominance. They probe ad infinitum the subtleties of our mind: "Why don't you use this product? Why don't you use that product? Why don't you go to this place? Why don't you go to that place?" It goes deep into the business mind of the chemical industry, or any shipper we presume, trying to establish this product in market competition. We are frankly scornful not of the questionnaires, but of the concept that brings them to us. We are very concerned about market dominance guidelines.

No. two, the Inflation Index. One of the Staggers Act's important contributions to the railroads' ability to improve their financial status was the provision—which we supported—assuring the carriers the opportunity to recover costs applicable to inflation. However, instead of developing its own cost index, the Commission adopted a price index largely based on the AAR price index. Use of this price index instead of the cost index called for in the act violates the Staggers Act, and the intent of the Senate as expressed in S. 1946. It substantially overstates costs actually incurred by the rail carriers. We urge the committee to direct the Commission to establish its own cost-based index instead of the price index now used.

The next point that we want to talk to is revenue adequacy. At this juncture, many railroads are experiencing record earnings. We believe many of the supposed revenue-inadequate carriers are healthy companies, obviously able to attract capital. My prepared remarks said there were three—I guess my friend Mr. Allyn may convince me that there are now only two railroads making money. Consequently we would submit that the subcommittee should review the Commission's revenue adequacy determinations.

In closing, I would say that CMA is greatly concerned with the actions taken by the Commission contrary to the intent of the act. Some of the steps reflect the view that the Staggers Act and S. 1946 were not regulatory reform, but established total deregulation. This is totally incorrect. We submit that your subcommittee

l use this occasion, this important hearing, to make that

ɜ statement follows:]

ENT OF DONALD G. GRIFFIN ON BEHALF OF THE CHEMICAL MANUFACTURERS ASSOCIATION

Chairman, and Members of the Subcommittee, my name is Donald G. Griffin. ice President of Distribution and Transportation of PPG Industries. With me s Gloria Sodaro, Staff Counsel for the Chemical Manufacturers Association

. appreciates the opportunity to appear today to present its views on the first der the Staggers Rail Act of 1980.

Chemical Manufacturers Association is a nonprofit trade association having ited States member companies representing more than 90 percent of the tion capacity of basic industrial chemicals within this country. Total ship- of chemicals and allied products were valued at $162.4 billion in 1980. s totaled $20.74 billion, representing 10.2 percent of the chemical industry's Approximately 45 percent of all chemical shipments are carried by rail. CMA y participated in the development of the Staggers Rail Act and has comment- and litigated many of the Commission's rules and regulations implementing t.

ll who participated in the effort last year to enact rail regulatory reform ion understand, the Staggers Rail Act of 1980 is the product of substantial mises by all parties. The object of the effort was to enact legislation which enable the railroads to improve their financial state, but at the same time continued regulatory protection for captive shippers.

. supported enactment of rail regulatory reform legislation because it believes strong, efficient and safe rail system is essential for the economic prosperity nation. CMA, therefore, supported greater rate flexibility, but cautioned that ually important to adequately protect captive shippers.[1] The Act ultimately had CMA's support because we believed it balanced the carriers' needs and ippers' interests, and that where regulation was being removed, competition take its place. Shipper interests, we believed, were incorporated in the rejec- the House provisions calling for almost total deregulation of rail rates; n of limited zones of rate flexibility and restrictions on the use of that zone ctober 1, 1984, to revenue inadequate carriers; adoption of the "Long-Cannon ment" enabling the ICC to place the burden of proof for rate increases above levels on the carriers; and inclusion of entry and reciprocal switching ons to enhance rail-to-rail competition. We also were greatly interested in rongly supported section 208, making it clear that shipper-railroad contracts ful and providing a mechanism for them to be approved by the Commission. provisions to maintain regulatory protection for captive shippers are of great ance because of the captive state of much chemical traffic. The traffic is for several reasons: First, the majority of our member company plants were l in order to use the U.S. rail system. Most of these are on a single line which s the only access to the rail system. Second, the industry has invested in rail cars. CMA companies own or lease over 100,000 cars, the replacement of which is approaching $5 billion. Third, many chemicals are restricted to cause of their bulk. These factors commit a very large segment of the al industry to rail transportation, and oftentimes to the one carrier serving a lar plant.

t is the chemical industry's reaction to the first year under the Staggers Act? hort, we have been greatly disappointed by the failure of the Interstate rce Commission to develop regulations to implement provisions in a manner ing the balance struck in the Act. We also are disturbed by several actions by the carriers to reduce competition, rather than increase it simultaneously e efforts to reduce regulation.

me first express our concerns about the Commission's implementation of the will address five subjects: (1) repeal of the market dominance presumptions placement by guidelines; (2) adoption of the AAR index as the inflation index; ICC's determination that no major carrier and only three railroads have e adequacy; (4) the railroads' proposal to, in effect, raise the jurisdictional old for the second year from a 165-percent revenue-to-variable cost ratio to

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[1] imony of CMA before the Senate Committee on Commerce, Science and Transportation, , 1980.

184 percent; and (5) calculation of the cost recovery percentage, for use beginning in 1984. Then, I will discuss how these rulings affect the attraction of the contract provisions in the Act, and conclude with comments on the decrease in rail-to-rail competition and the Commission's rail cargo liability study.

1. MARKET DOMINANCE

On July 8, 1981, the ICC issued orders rescinding the market dominance rules that had been in effect since 1976.[2] These rules established presumptions of market dominance for shippers to satisfy. Most important to the chemical industry were the market share test and the substantial investment test. Despite the protests of CMA and other shipper groups, the ICC removed the presumptive tests and replaced them with evidentiary "guidelines." Further, it included product and geographic competition among the issues on which the guidelines seek evidence.

We believe these ICC orders violate both the 4-R Act of 1976 and the Staggers Rail Act. The removal of the presumptions and their replacement with indefinite guidelines violates the command in section 202 of the 4-R Act that the ICC adopt by rule "standards and procedures," and that "such rules shall be designed to provide for a practical determination without administrative delay." We are pleased that this point recently has been recognized by ICC Chairman Taylor. Reflecting on the Commission's obligations under section 202, he said:[3]

". . . I must question whether the new evidentiary criteria is consistent with our original Congressional mandate that we establish 'standards and procedures' that, with regard to market dominance, will permit 'a practical determination without administrative delay.' Certainly, if our former presumptions could be characterized as crude and not always accurate, our present criteria could be characterized as something less than totally objective and unambiguous."

We consider the Commission's decision to consider product and geographic competition to be unlawful and in excess of statutory authority. That decision reverses the Commission's previous position that the 4-R Act did not authorize consideration of product and geographic competition as part of market dominance—a position that was sustained by the U.S. Court of Appeals for the D.C. Circuit.[4]

The Commission's July 8, 1981 orders make clear that the Commission places exclusive reliance for its new approach on the "intent of the Staggers Act." Yet, no provision of the Staggers Act supports the Commission's change of position; if anything, the Staggers Act expressly disclaims any change in the meaning of market dominance. As importantly, the intent of Congress, as evidenced by the legislative history, shows a desire to exclude these very considerations from market dominance proceedings. Proposals to specifically direct the Commission to include product and geographic competition were twice rejected—once by the Senate Committee on Commerce, Science and Transportation (when, after hearings, it rejected the previous Administration's bill (S. 796)),[5] and once by the House of Representatives (when the rate provisions in H.R. 7235 fell to the "Eckhardt-Rahall Amendment"). Nonetheless, the Commission's market dominance guidelines seem premised on those measures that failed enactment.

One result of the Commission's guidelines has been a series of interrogatories, in the guise of inquiries about product and geographic competition, that seek specific information on how the chemical industry is conducted, as well as very sensitive proprietary information. It is our view that these questions have no relevance to the issue of whether a particular rail rate is reasonable. I think the Committee may be interested to review the kinds of questions that the railroads are asking in an effort to establish product and geographic competition. (See Attachment A.)[6]

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[2] Ex Parte 320 (Sub-No. 2), Market Dominance Determinations and Consideration of Product Competition, 45 Fed. Reg. 35098 (1981).

[3] Id., concurring opinion in decision denying petitions for reconsideration; order served Oct. 28, 1981.

[4] *Atchison, Topeka and Santa Fe Ry. Co.* v. *Interstate Commerce Commission*, 589 F. 2d 623 (D.C. Cir. 1978).

[5] At hearings in May and June, 1979, before this Committee, shippers expressed a strong negative reaction to S. 796 because it provided little or no protection for captive shippers, with particular opposition to the provision in S. 796 on product and geographic competition. CMA testified that it found "[p]articularly objectionable . . . a requirement to determine the existence of alternative markets and the definition of a reasonable transportation alternative. We fear that placing these burdens on the shipper will result in an effective denial of maximum rate protection for the captive shipper." Railroad Deregulation Act of 1979: Hearings Before the Subcommittee on Surface Transportation of the Senate Committee on Commerce, Science and Transportation, 96th Cong., 1st Sess. (1979) at 746 (Statement of Donald G. Griffin).

[6] Attachment A has been retained in the committee files.

CMA and many other parties are in the process of litigating these questions in the U.S. Court of Appeals for the Fifth Circuit. (*Western Coal Traffic League* v. *United States,* Nos. 81-4257, *et al.*) While we are confident that the court will uphold our legal position, it is important that this Committee be cognizant of the action taken by the Commission and its consequences. To us, the orders removing the presumptions and adopting guidelines make it much more difficult than Congress ever intended for shippers to procure review of rail rates and upset the careful railroad-shipper balance that this Committee and other members of Congress worked so hard to achieve last year.

2. INFLATION INDEX

One of the Staggers Act's important contributions to the railroad's ability to improve their financial status was the provision, which CMA supported, in section 203 assuring the carriers the opportunity to recover costs attributable to inflation. The Act and its legislative history make it clear that "inflation increases" are to be based on an index adjusted to reflect cost changes in the mix of expenses incurred by railroads.

We call the Subcommittee's particular attention to this because section 203 is based on the Senate bill, S. 1946.[7] A colloquy between Senator Cannon and Edmund Frost (General Counsel of CMA) on the need to delete references in the initial version of S. 1946 to the AAR's Index of Railroad Material Prices and Wage Rates and replace that with "appropriate adjustments to reflect the changing composition of railroad costs, including the quality and mix of material and labor" shows the intent of the Committee and of Congress: to employ an index based on costs which reflect changes in traffic volume, productivity and other relevant factors.[8]

However, instead of developing its own index, the Commission has decided to use a composite of the Producer Price Index and the AAR price index. Use of this index, which does not reflect improved productivity or larger traffic volumes, violates the Staggers Act and the intent of the Senate as expressed in S. 1946, and overstates costs actually incurred by rail carriers. This overstatement of inflation is quite substantial. Over the 10-year period 1969 to 1979, the composite price index advocated by the Commission would have reflected an annual change of 10.25 percent in the cost of doing business, while the experience of the railroads indicates an annual change of only 7.43 percent.[9] This would have been approximately 36 percent more than the railroads were entitled to.

While we continue to be greatly concerned about this issue, we appreciate the fact that our concerns have attracted the attention of ICC Chairman Taylor. Labelling the Commission's adoption of the AAR index as an expedient and noting that a cost index would be more difficult to develop, the Chairman expressed his "reservations as to whether this [the AAR index] is the type of index envisioned by the statute."[10] For these reasons, we urge this Subcommittee to direct the Commission to establish its own inflation index, instead of the index now in use.

3. REVENUE ADEQUACY[11]

One of the key policy determinations made in the Staggers Act was that those carriers not earning adequate revenues should be granted more rate flexibility than those with adequate revenues. Thus, a distinction was made on this basis in section 203 of the Staggers Act with respect to the availability of the 4 percent rate flexibility zone. The question of whether a carrier is revenue adequate also has been an important consideration in rulemaking and individual rate cases. The railroads argue that it has bearing on the amount the Commission should allow a captive shipper to be charged.

At this juncture, many railroads are experiencing record earnings, and several are diversifying into other industries. According to the Wall Street Journal, a provision in the 1981 tax law enables the railroads "to start writing off, this year,

[7] According to the House-Senate Conference Reports, computation of the rail cost adjustment factor is contemplated "as contained in the Senate bill." Conf. Rep. on Staggers Rail Act, H. Rept. No. 96-1430, 126 Cong. Rec. H9918 (daily ed., Sept. 29, 1980).

[8] Hearings on S. 1946 before the Senate Committee on Commerce, Science and Transportation, 96th Cong., 1st Sess. (1979) at 528-530.

[9] Verified Statement of Gerald W. Fauth, referenced in Brief of Petitioner CMA in the case captioned *Western Coal Traffic League, et al.* v. *United States* (D.C. Cir. Nos. 81-1437, *et. al.*)

[10] 46 Fed. Reg. 48939 (Oct. 5, 1981).

[11] The ICC's decision in Ex Parte No. 393, Standards for Railroad Revenue Adequacy is before the courts in *Chemical Manufacturers Association* v. *United States,* (D.C. Cir. No. 81-1521).

about $8 billion in railtrack, some of which has been carried on the books since 1887." Continuing, the article says:

"Consequently, the railroads are busy trying to decide how to use all the cash. It can go into new facilities, the repayment of high-cost debt, investment in high-yielding securities, or acquisitions of nonrailroad companies." [12]

Nonetheless, the Commission has determined that only three carriers are revenue adequate. This decision departs, without justification, from its determination under previous standards of revenue adequacy that 13 Class I railroads were revenue adequate and others were on the edge of achieving that status.[13]

We urge the Subcommittee to review the Commission's revenue adequacy determinations, and compare them to the intent of the Staggers Act. We think the Subcommittee will find that many of the revenue inadequate carriers are healthy companies, quite able to attract capital. Such carriers should not enjoy the subsidies the Staggers Act offers to carriers truly not earning revenues adequate to attract capital.

4. RAILROADS' PETITION TO EFFECTIVELY RAISE JURISDICTIONAL THRESHOLD FOR SECTION 229 COMPLAINTS FROM 160 TO 184 PERCENT

Last March, a number of chemical companies filed complaints against existing rates pursuant to the transition provisions in section 229 of the Staggers Act. When those complaints were filed, the jurisdictional threshold was 160 percent of variable costs.

The railroads have recently petitioned the Commission to declare, in effect, that the threshold for these complaints is 184 percent and have asked for the dismissal of all cases where the revenue-to-variable cost ratio is below that figure.[14] In addition, the railroads contend that the Commission must determine whether a rate is below the threshold on the basis of unadjusted Rail Form A costs.

Numerous complainants responded on October 16, 1981, arguing, among other things, that the railroads' petition is an effort to eradicate the numerial jurisdictional thresholds established in the Staggers Act as the result of compromises reached after a lengthy legislative struggle. The railroads' position, the shippers argue, would now change the rules and deprive shippers (in section 229 cases and subsequent cases) of the right to Commission review of rates yielding revenue/cost ratios of 160 percent-183 percent—a right that they and, I believe, this Committee believed had been provided by the Staggers Act.

A group of shippers also addressed the railroads' effort to base costs for jurisdictional inquiries solely on unadjusted Rail Form A.[15] They establish in their filing that the railroads' position is contrary to Congress' intent, as expressed in section 10709(d)(3)[16] and in the legislative history, that revenue-to-variable cost ratios be based on the actual cost of the particular movement, not on a railroad's unadjusted system-wise costs found in Rail Form A.

These matters are now before the Commission. Because they raise serious issues as to whether Congress' intent is being followed, it is important that the Subcommittee oversee them.

5. COST RECOVERY PERCENTAGE

Under the Staggers Act, the cost recovery percentage (CRP) will be taken into account to establish the jurisdictional threshold, beginning in 1984. The Commission has stated that once the costing methodology for this figure is chosen, the CRP will be published without an opportunity for comment. We believe that this aproach would improperly bypass the Administrative Procedure Act by depriving parties an opportunity to comment on this standard.

In summary, CMA is greatly concerned by actions taken by the Commission contrary to the intent of the Staggers Act. Several of these steps reflect the view that the Staggers Act, and the Senate bill (S.1946), were not regulatory reform measures—but rather established total deregulation. This is totally incorrect. This Subcommittee should use the occasion of this important hearing to make that clear.

Now, I would like to discuss the contract provision, and its direct relationship to maximum rate regulation.

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[12] Attachment B retained in committee files.

[13] Ex Parte 353; 362 ICC at 303.

[14] Railroads' Petition to Replace Cost Updating Methodology, and Motion to Dismiss Certain Complaints in Ex Parte 411.

[15] Petition for a Declaratory Order (filed Oct. 26, 1981) in Ex Parte 411.

[16] The relevant statutory language is ". . . revenue-variable cost percentage for a particular transportation."

Contracts

The actions in the ratemaking area by the Commission that I have discussed have a direct bearing on use of the contract provisions in the Staggers Act. Section 208, which established the legality of railroad-shipper contracts, was strongly supported by CMA and its members. In urging enactment of this provision, the chemical industry viewed contracts as a means of providing carriers with assured long-term sources of revenue, and shippers with an assured quantity and quality of service.

To date, there have not been many rail-chemical shipper contracts. There appear to be several reasons for this: First, contracts are the result of two parties' efforts to define their mutual interests. The Commission's signals, such as the market dominance guidelines, that there will be limited rate regulation significantly mitigates the carriers' incentive for contracts. Why should the carriers commit themselves in a contract to a rate when the Commission shows unwillingness to monitor even captive rates?

The second factor is the problem of negotiating a contract for a joint movement. The railroads' age-old disputes over divisions are a stumbling block to consummation of a contract on a joint movement.

Finally, the absence of Commission regulations implementing section 208 appears to be slowing the carrier's willingness to seriously negotiate contracts.

In CMA's view, the contracts provision is one of the most important measures in the Act. But, to be effective, it must be accompanied by effective regulation of rates for captive shippers.

Decrease in rail-to-rail competition

Measures in the Staggers Act to facilitate increased rail-to-rail competition (entry, section 221, and reciprocal switching, section 223) have hardly been used. While there have been instances of increased competition, such as TOFC/COFC, overall the first year under the Staggers Act has witnessed a reduction, rather than an increase in rail-to-rail competition. This is the result of mergers, as well as cancellations by carriers like ConRail and the Family Lines of joint rates where these carriers have either the original or terminal movement.

Rail carrier cargo liability study

Finally, CMA is pleased with the Commission's "Rail Carrier Cargo Liability Study," which was submitted to Congress last month. We support and urge adoption of the Commission's three recommendations: Elimination of the venue restrictions in the Staggers Act; granting the courts authority to award attorneys' fees to successful claimants; and removal of the $10,000 jurisdictional threshold for access to federal courts.

I appreciate this opportunity to appear before the Subcommittee, and am prepared to attempt to answer any questions the Chairman or Members may have.

Thank you.

Senator DANFORTH. Thank you, gentlemen. We appreciate your testimony.

The next panel is an agricultural panel—Edwin M. Wheeler, Paul Stepner, and Fred Zitto.

STATEMENTS OF EDWIN M. WHEELER, PRESIDENT, THE FERTILIZER INSTITUTE; PAUL STEPNER, CHAIRMAN, TRANSPORTATION COMMITTEE, NATIONAL GRAIN & FEED ASSOCIATION; AND FRED M. ZITTO, REPRESENTING AMERICAN PAPER INSTITUTE, ACCOMPANIED BY JOHN F. DONELAN, ESQ., TRANSPORTATION COUNSEL, AMERICAN PAPER INSTITUTE

Mr. WHEELER. Good morning, Senator. For the record, my name is Edwin Wheeler. I'm the full-time president of the Fertilizer Institute located here in Washington, D.C.

Very quickly, we're in the same situation as is the coal industry. We are captive in the sense that we cannot move our mines. Let me give you a classic. In the State of Florida we're producing 50 million tons of material a year, all captive to one railroad, the Seaboard Coast Line. In Carlsbad, N. Mex., we produce about 2¾

million tons of potash, all captive to the Santa Fe. So it goes. The big mines up in Idaho—all captive to the Union Pacific.

We worked, as did the other gentlemen on this panel, for the Staggers Act. We felt that deregulation was long overdue and spent a lot of time lobbying on it. The Staggers Act, as interpreted by the Interstate Commerce Commission is now going in a direction the Congress never intended. That is to say, the railroads are soon going to have a monopoly in our industry rather than a market dominance. We cannot move the mines. We cannot move our former customers. Railroads are simply putting a pistol to our head on rates and are driving the cost of material up, up, and up. Our rail bill last year was about $1,500 million. That means the Nation's farmers are paying a terrific transportation bill.

This morning I want to review with you, and I'll stay within the time frame, three points.

No. 1, the Commission is not following the law on the question of market dominance. They've decided now to come up with new rules, the so-called geographical tests, and so forth, but the Congress made it clear to the Interstate Commerce Commission that where they had us by the throat, and they do in our industry, then certain rules were to be followed, which they have just willy-nilly put aside. The hearings thus far before the Interstate Commerce Commission remind me of a little Indian boy that came out of the movie out in a small town in Wyoming. He looked up at his father and said, "Don't we ever win?" And that's the way the shippers feel with the Interstate Commerce Commission.

Moving on quickly, we are being plagued by wholesale branch line abandonments, because the bulk of our fertilizer retailers are located on branch lines. The carriers are making the argument with great success that they can't keep it on the marginal lines, but that they can make better alternative uses of their money and are pulling these lines out and selling them for scrap. The alternative use though is not necessarily going into the balance of the rail plant. It's going into buying Coca-Cola bottling franchises, Midas Muffler, et cetera, et cetera.

So, in effect, we're being deprived of service to support nonrail activities.

If they can't pull the track up, they are imposing surcharges on cars moving over the branch line. Recently one of the carriers established $1,044 per car surcharge over and above the normal rate. We don't believe the Congress ever intended for the rail lines to just wholesale abandon the rural areas of the United States.

In the rate hearings we are at the mercy of the railroads on their costs. There's no way in the world we can reconstruct their costs. One of the things I personally lobbied hardest on in the Staggers bill was to get a railroad accounting principle board established and put the railroads on 1981 accounting methods. Thus far, the Congress had not funded that board, and you can bet your bottom buck, the AAR doesn't want it funded. We think it's curious that they're so strongly against a new modern accounting system. We think we know what the answer is, but nevertheless, I would hope that the committee reports to the full Senate that the accounting board should now be funded.

Last but not least, Senator, I invite your attention to my testimony, where in a recent article in Forbes magazine, two railroad presidents said that they believed by 1990 there will only be six carriers serving the United States. The way they're going now, there isn't any doubt that's what's going to happen. We will have the biggest monopoly in six companies that has ever been seen in our history. If the ICC is not directed to get back on the Staggers Act, we are going into one serious situation.

Thank you, sir.

[The statement follows:]

STATEMENT OF EDWIN M. WHEELER, PRESIDENT, THE FERTILIZER INSTITUTE

We understand that the Subcommittee on Surface Transportation wishes for the testimony today (November 10, 1981) to be limited to the implementation by the ICC of the Staggers Rail Act of 1980. Therefore, we will limit our discussion of possible legislative changes to the Act until Congress convenes the appropriate hearings.

First, we wish to point out that our comments today are not directed at the ICC Chairman Reese Taylor. It is too early to assess the effect Mr. Taylor's presence will have on the Commission or on the Commission's implementation of the Staggers Rail Act. We do, however, hope that Mr. Taylor means what he says when he states that while he adheres to the philosophy of deregulation, he intends to act according to what he believes was the intent of Congress as expressed in the statute.

By way of background, TFI in general supported the Staggers Act and what we believed to be its primary purpose, to encourage a financially strong railroad common carrier system under private ownership, while at the same time balancing the needs of carriers and the shipping public. We supported the legislation because we believed Congress had written into the Act various provisions designed to protect captive shippers.

The fertilizer industry represented here today by its trade association, The Fertilizer Institute, is a classic example of the captive shipper. Our Institute represents approximately 95 percent of basic fertilizer production in the United States. Our industry delivered over 55 million tons to U.S. farmers as well as exported in excess of 29 million tons and imported well over 14 million tons in the year ending June 30, 1981. We produce from mines in Florida, North Carolina, and Idaho, nearly 60 million tons of phosphate. Shipped as either "rock" or finished product, these materials are 70-90 percent rail-hauled and, except in North Carolina, can be characterized as "captive," in that only one rail carrier is involved at the point of orgin. Potash—another major product of the fertilizer industry—is captive in that the bulk of U.S. potash originates on one railroad that serves the Carlsbad, New Mexico mines.

Perhaps the most publicized reason given for the need and passage of the Staggers Act was to meet the increased capital needs of the railroads. However, Congress had several purposes and goals for passing this legislation:

First, to assist the railroads of the Nation in rehabilitating the rail system in order to meet the demands of the interstate commerce and the national defense.

Second, to reform federal regulatory policies so as to preserve a safe, adequate, economical, efficient and financially stable rail system.

Third, to assist the rail system to remain viable in the privater sector of the economy.

Fourth, to provide a regulatory process that balances the needs of carriers, shippers, and the public.

Fifth, to assist in the rehabilitation and financing of the rail system.

Frankly, in our judgment the ICC has in their decisions lost sight of these goals, except to assist in the rehabilitation and financing of the rail system. Certainly, from profit statistics currently available, the U.S. rail system has a better profit picture than it has had in years. The AAR reported an increase in their ordinary net income of nearly 300 percent for the Nation's railroads, including Conrail, for the first quarter 1981, as compared to the same period one year ago.

The majority of the railroads in the United States, with the exception of Conrail and a few others, are experiencing a huge increase in profits. In this "recessionary time" while most industries are closing plants and laying off employees, the Norfolk and Western, for example, has just reported the highest net revenue for any quarter in its history. The Southern Railroad, proposed merger partner of the N & W, reported record earnings also for the same period. I.C. Industries, a holding com-

pany for the Illinois Central Gulf, just bid $454 million for a household appliance company. I could cite other cases; however, I believe the picture is complete, the railroads have indeed increased their revenue earnings.

What is confusing, however, is to compare railroad financial statements circulated on Wall Street with the ICC's assessment of whether railroads are receiving adequate revenues. With the exception of three small railroads, all the railroads in the country are still classed by the ICC as "revenue inadequate" railroads. From any commonsense standpoint, this assessment is utterly ridiculous and indicates ICC's singlemindedness toward increasing rail revenue.

The ICC, in implementing the provisions of the Staggers Act, operates under the assumption that the marketplace regulates more efficiently and more fairly for the public good than the government does. Indeed, a spokesman for the Commission has indicated to fertilizer shippers several times that they should act in the marketplace as if the ICC does not exist. This may work in certain transportation areas, such as in the trucking and airline industry. However, it does not necessarily follow that the same result will be achieved in the railroad industry. Entry for new railroads into the rail system simply does not occur as in the trucking and airline industry. Railroads were granted eminent domain over the land upon which their track stands, only they can use those tracks, and costs associated with building a new track system are astronomically high and inhibit new rail competition.

The ICC believes that the rail marketplace is the cure-all for rail transportation. We submit, however, and the evidence indicates, that we are rapidly approaching the time and place where no such marketplace exists in the context of rail transportation.

Railroad mergers, exempt from antitrust laws, are proceeding at a rapid pace. As indicated in an article in Forbes for November 9, 1981:

"Both Claytor (N & W president) and Hall (Southern Railroad President) believe that the Nation's rail system will be consolidated in fewer and fewer hands over the next decade. By the 1990's there may be only six giant corporations—compared to more than a dozen major players at present."

Hand in glove with the merger activities, these already giant corporations are cancelling joint routes and rates with other railroads in order to force shippers located on the originating carrier's line to use that line to the greatest extent possible.

If there are to be only six giant railroad systems, as the President of N & W and Southern have suggested, and if each system is to be permitted to restrict shippers on its line to use of that carrier's long-haul route—preventing the shippers from using competitive carriers—then what we have created is not a government-supported marketplace, but a government-created monopoly.

Adding to our concerns over this government-created monopoly is the alarming rate at which railroads are abandoning track. Obviously, track that is non-productive and not generating revenues should be abandoned and the Staggers Act clearly establishes procedures to speed up the abandonment process as long as "the present or future public convenience and necessity require or permit the abandonment."

The ICC clearly is in favor of abandonments. Over a period of 25 months beginning August 1, 1979, the Commission granted 330 abandonment applications in a row until the string was broken by the decision served September 16, 1981, prohibiting the Chicago Northwestern Railroad from abandoning a line in Illinois. In addition, the ICC through its inaction, is allowing companies to abandon track because they earn a greater return on their investment in land and track materials by investing in non-railroad use. This system deals with the so-called "opportunity cost" doctrine. Under this concept, railroads are encouraged to abandon many profitable branch lines and to invest the capital in non-railroad use. Encouraging disinvestment in railroad branchlines are, at the least, highly questionable as a matter of national transportation policy and definitely does not embody congressional intent as enunciated by the Staggers Act. Does the Senate endorse a policy which permits the Illinois Central Gulf Railroad, for example, to abandon a moderately profitable branchline under the theory that it can make more profit by scrapping the track and investing the proceeds in Midas Muffler or a soft drink operation? We think not.

Furthermore, contrary to explicit legislative intent, the Commission is permitting the railroads to use branchline surcharges to effect the de facto abandonment of railroad lines. Branchline surcharges have been assessed in amounts up to $1,004 per car (ICG Cherokee Branch) which makes the railroad charges to the shipper prohibitive.

We are further concerned that railroad holding companies seem to have more interest in their mineral and timber holdings or in purchasing other companies than they have in running their railroad. One of the goals of the Staggers Act was

to increase rail revenues in order to rehabilitate the rail system. However, instead of rehabilitating the system, holding companies are abandoning track in need of renovation and are taking the money and investing it in non-rail use. Congressman Brian Dorgan of North Dakota recognizes the serious problems this could create for the rail transportation system in the United States and, along with Representative Pat Williams of Montana, are campaigning to require holding companies to direct part of their revenues from land grant developments to support rail facilities. As long as holding companies constantly transfer rail funds to non-rail use, in the eyes of the ICC at least, there will never be a revenue-adequate railroad.

The fact that the ICC has lost sight of the goals, established by Congress in implementing the Staggers Act is very evident in the Commission's decision in Ex Parte 320 (Sub. No. 2), "Rail Market Dominance." The Commission held in this case that it would consider evidence of geographic and product competition in making determinations of market dominance. The Commission is basically saying that only under very, very few instances is there such a thing as market dominance. If this is true, why then was there ever a need for the Interstate Commerce Commission and why was the Interstate Commerce Act passed in 1887?

Every student of transportation knows that the purpose of the Interstate Commerce Act was to cut up by the roots every form of discrimination, favoritism, and inequality. In this decision, the ICC basically says that there is no reason for the Interstate Commerce Commission to exist. We submit that Congress intended to protect captive shippers under Staggers and not to remove all rail rate jurisdiction from the ICC.

The importance of cost status in the regulatory process has been constant throughout the history of the ICC, and even more important in the provisions of the Staggers Act.

Not only did the role of cost become ever more important under the Staggers Act, but the availability of such data was regarded as being essential for the protection of shippers in the arena of rate negotiations, where previously there had been regulatory protection.

For these purposes, two new accounting systems have been adopted by the Commission. They are the Uniform System of Accounts (USOA) and the Uniform Rail Costing System (URCS).

The Uniform System of Accounts allows wide discretion to the railroads as to how they may record their expenses, and provides almost no check against either mistake or deliberate, erroneous allocations. Thus, the railroads are able to make purely arbitrary allocation costs against particular services or kinds of traffic to the extent they choose to do so. There is almost no auditing of accounts by the ICC, since it does not have sufficient money to hire auditors. Yet, this system of accounts is supposed to produce the data upon which the new Uniform Rail Costing System is to be based.

Congress sought to assist the ICC in developing cost information by enacting Section 302(a) of the Staggers Act. The Staggers Act reads, in part, to "establish a railroad accounting principle board which shall be within and responsible to the legislative branch of the federal government." Enactment of the foregoing provision was a part of a compromise offered to shippers in return for their support of the Staggers Act. So far, however, funds to create the Railroad Accounting Principles Board have not been appropriated by Congress.

Although the board was "established" as necessary to protect shippers by providing reliable accurate determinations of costs, no one has been appointed to the board and it is not functioning.

In order that the shipping public may get the necessary costing information from the railroads, it is imperative that the new Railroad Accounting Principle Board be staffed and funded to assist the ICC in developing the necessary costing data required in the Staggers Act.

Senator DANFORTH. Thank you. Mr. Stepner?

Mr. STEPNER. Mr. Chairman, my name is Paul Stepner, vice president of transportation of the Pillsbury Co., Minneapolis, Minn., chairman of the transportation committee of the National Grain and Feed Association.

I enter this statement on behalf of the association. The National Grain and Feed Association is a voluntary association of grain and feed firms ranging in size from the smallest country elevator to the largest grain and feed complex. It includes merchandisers, processors, warehousemen, and exporters of a wide spectrum of grains

and feeds. Its membership includes 1,250 direct members by individual firms and 46 State or regional grain and feed associations affiliated with the national association, including some 10,000 grain and feed firms.

Although it is too early to judge the long-range effects of the Staggers Rail Act of 1980 on carriers and shippers, the National Grain and Feed Association believes there are certain features of the act that are of major concern to the grain and feed industry and have a detrimental effect on the orderly marketing of grain and grain products. Three areas of particular concern are spelled out in my text. Briefly, they are as follows:

First, contract rates. The National Grain and Feed Association believes there should be full disclosure of terms and provisions of rail contracts on agricultural commodities. Such terms and provisions should be disclosed in their entirety at the time the contract is filed, so that full force can be given to the Staggers Act provision under which a complaint over a contract can be filed with the Interstate Commerce Commission, if the contract will result in unreasonable discrimination, destructive competitive practices, or failure of the carrier to meet its common carrier obligation. The ICC has initiated a rulemaking procedure, Ex Parte 387, on rail contracts on which the National Grain and Feed Association has submitted comments in support of full disclosure of contract terms.

Should the ICC fail to require such disclosure, the association believes that the Staggers Act should be amended to specifically require full disclosure of contract terms, so as to offer competing shippers the protection which Congress intended under the act's contracts provisions. An agricultural shipper is entitled to know all the economic terms contained in a competitor's rail contract before he can exercise effectively his rights under the statutes. The railroads have refused to disclose sufficient contract information voluntarily, when shippers have requested it for the purpose of entering into similar contracts.

Second, demand-sensitive rates. The National Grain and Feed Association believes that the entire subject of demand-sensitive rates and rate changes on short notice should be reviewed. The association believes that the ICC needs to consider more carefully the intent of Congress when approving rate tariffs and contracts for agricultural commodities that are of a demand-sensitive nature. Demand-sensitive rates for agricultural commodities are expressly forbidden under section 209 of the Staggers Act. Additional legislative emphasis may be required in the future, because this issue has a direct and a disruptive impact on the grain marketplace.

Since enactment of the Staggers Act, the grain industry has continued to be subjected to the implementation of rates that are of a periodic and demand-sensitive nature.

Third, adequate notice of rate changes. Rail carriers continue to have great difficulty in keeping shippers adequately apprised of rate changes under the timeframe mandated by the Staggers Act. The association believes that rail carriers should be responsible to make certain shippers have adequate notice of rate changes. The change in notice to 10 days for rate decreases and 20 days for rate increases can be beneficial to railroads and shippers alike. Unless

shippers know their transportation costs at the time of shipment, grain marketing will be affected adversely.

Thank you, Mr. Chairman.

[The statement follows:]

Statement of Paul Stepner on Behalf of the National Grain and Feed Association

Mr. Chairman and Members of the Subcommittee, my name is Paul Stepner. I am Vice President of Transportation for the Pillsbury Company of Minneapolis, Minnesota. I am Chairman of the Transportation Committee of the National Grain and Feed Association and enter this statement on behalf of the Association.

The National Grain and Feed Association is a voluntary association of grain and feed firms ranging is size from the smallest country elevator to the largest grain and feed complex and includes merchandisers, processors, warehousemen, and exporters of a wide spectrum of grains and feeds. Its membership includes 1,250 direct memberships by individual firms and 46 state or regional grain and feed associations affiliated with the national association, including some 10,000 grain and feed firms.

The Staggers Rail Act of 1980, effective on October 1, provides sweeping changes in rail regulation. Although it is too early to judge the long range effects of this legislation on carriers and shippers alike, there is no doubt that the Staggers Act has resulted in significantly reducing rail carrier regulation. There are certain features of the Act which concern the grain and feed trade and have a detrimental effect on the orderly marketing of grain.

Contract rates

The National Grain and Feed Association's transportation policy states "we are not opposed to the concept of contract rates for rail transportation, providing safeguards under the interstate Commerce Act and Anti-Trust Laws are carefully adhered to. We support the full disclosure of terms and provisions of contracts on agricultural commodities."

Section 208 of the Staggers Rail Act of 1980 establishes a new statutory provision. This section specifically permits railroads to enter into contracts with purchasers of rail services, to provide specified services under specified rates and conditions.

Among other provisions, the act requires that each contract shall be filed with the Interstate Commerce Commission, together with a summary of such non-confidential information as the Commission prescribes.

The grounds for complaining against contracts are set forth in 49 U.S.C. 10713(d)(2), and are as follows:

"(2)(A) In the case of a contract other than a contract for the transportation of agricultural commodities (including forest products and paper), a complaint may be filed—

"(i) by a shipper only on the grounds that such shipper individually will be harmed because the proposed contract unduly impairs the ability of the contracting carrier or carriers to meet their common carrier obligations to the complainant under section 11101 of this title; or

"(ii) by a port only on the grounds that such port individually will be harmed because the proposed contract will result in unreasonable discrimination against such port.

"(B) In the case of a contract for the transportation of agricultural commodities (including forest products and paper), *in addition to the grounds for a complaint described in subparagraph (A) of this paragraph, a complaint may be filed by a shipper* on the grounds that such shipper individually will be harmed because—

"(i) the rail carrier has unreasonably discriminated by refusing to enter into a contract with such shipper for rates and services for the transportation of the same type of commodity under similar conditions to the contract at issue, and that shipper was ready, willing, and able to enter into such a contract at a time essentially contemporaneous with the period during which the contract at issue was offered; or

"(ii) the proposed contract constitutes a destructive competitive practice under this subtitle." (Emphasis added.)

The Interstate Commerce Commission has initiated a rule making proceeding in connection with railroad transportation contracts (Ex Parte 387). The National Grain and Feed Association submitted comments in this proceeding, and at the time this statement was written the Commission had not published its decision.

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It is the position of National that contracts involving the transportation of agricultural commodities must be disclosed in its entirety at the time the contract tariff is filed in order to give full effect to the provision under which a complaint may be filed. A shipper must know all of the economic terms which have been made available to its competitor before that shipper can effectively exercise his rights under the statute.

Unless full disclosure of all terms and conditions is required, it is virtually impossible for a shipper to claim discrimination on the part of a carrier refusing to enter into a similar contract. Nor can a shipper determine if the proposed contract constitutes a destructive competitive practice. Without full disclosure, the competing shipper is placed in a "Catch 22" position. In fact, railroads have refused to disclose sufficient information when shippers have asked for such information for the purpose of entering into a similar contract.

Should the Commission not require full disclosure of contract terms and conditions in Ex Parte 387, the Interstate Commerce Act should be amended to specifically require such disclosure. This would offer competing shippers the protection which Congress intended under the contract provisions of the Staggers Act.

Demand-sensitive rates

The National's transportation policy covers demand-sensitive pricing as follows:

"The association is opposed to the use of demand-sensitive transportation pricing on agricultural commodities on short notice which has adverse effects on the orderly marketing of grain."

As a result of our efforts, as well as those of others, protection was provided in the final drafting of Staggers for agricultural commodities against any kind of demand-sensitive pricing. The specific language reads as follows:

DEMAND-SENSITIVE RATES

"SEC. 209. Section 10727 of title 49, United States Code, and the item relating to such section in the section analysis for chapter 107 of such title are repealed."

The conference report further enlightens the record and strongly indicates Congress' intent as shown below:

SECTION 209—DEMAND-SENSITIVE RATES

"*Senate bill.* The Senate bill amends 49 U.S.C. 10727 to provide for the filing of demand-sensitive tariff in response to explicit or anticipated fluctuations in demand for rail services. The tariff would apply to a maximum and minimum rate regulation. The Senate bill specifically excluded grain from this provision.

"*House amendment.* The House amendment repealed 49 U.S.C. 10727 because of the concerns raised by agriculture interest groups about the way demand-sensitive tariffs had been implemented. The provision was originally included in the 4-R Act to provide greater car utilization by encouraging rail shippers to ship in off-peak, low-demand periods. The repeal of the demand-sensitive tariff authority should not be construed by the Commission as a resolution of the car utilization problems. The Commission has other ways to abate the serious problem of the declining car utilization in the rail industry.

"*Conference substitute.* The conference substitute adopts the House provision. The conferees direct the Commission to explore alternative methods of improving car utilization and making railroad prices and services more responsive to market conditions instead of artificial regulatory restraints. *However, the Commission is on specific notice not to contravene the policy set out by Congress which is clearly to prevent demand-sensitive rates by any means to apply to agricultural commodities.*"

Despite the strong language in the conference report and obvious intent of Congress that demand-sensitive rates of any kind were not to apply to agricultural commodities, we see rates being implemented that are periodic in nature. While it might seem that these changes are aimed at short-term changes in demand for rail grain service, more often than not, they are merely "knee-jerk" reactions by carriers in reaction to each other's rate cuts, or top management's orders to do something about the surplus of rail cars. All of this has an adverse effect on grain prices and the grain market in particular; and are, in our opinion, direct violations of Section 209 of Staggers that prohibits any kind of demand-sensitive rates.

Some examples of these rate activities include the following areas:

A. Contract rates such as a Southern Railway contract, which allows for rebates based on railroad equipment loaded as a percentage of prior business, during times of car surplus.

B. Contracts and rates being put into effect, where there is obvious market impact, on short notice, usually only one day.

C. Branch line surcharges of short duration.

D. Rate decreases or discounts to stimulate demand in a marketplace where railroad rate changes can have little, if any, effect on foreign or domestic demand.

In the Southwestern section of the country in particular, we are experiencing so many changes so quickly (many on one day's notice), that neither carriers nor shippers know what is going on. We are seeing carriers reacting to lower grain exports and the resulting surplus of hopper cars with secret contract rates and rate cuts which are to the detriment of the grain marketplace as well as themselves. While it may seem that railroads are becoming more market oriented, actually the reverse is happening in that they are not at all meeting the needs of the marketplace. The net result on the grain marketplace is a refusal by many parties to forward contract and an inability of the grain marketplace to function as it normally does, as the railroads engage in destructive competition.

While the intent of Congress was clear, we feel that this entire area of demand-sensitive rates and rate changes on short notice needs to be reviewed. We suggest that the I.C.C. needs to more carefully consider the intent of Congress in approving rate tariffs and contracts which carry demand-sensitive rates on agricultural commodities. We intend to discuss this with the Commission. Since this issue has a definitive impact on the grain marketplace, additional legislative emphasis may be required for the future.

Adequate notice

The National's position on adequate notice states, "Railroads should be required to provide to shippers notice of transportation changes to protect orderly marketing of grain."

Section 10762(c)3 of title 49, U.S. Code was amended providing for 20 days' notice on rate increases and 10 days' notice on rate decreases. Previously 30 days' notice was required.

The railroads are having great difficulty keeping shippers apprised of rate chagnes. It is not unusual to have new rates in effect before shippers receive the new tariffs or supplements. We are working with the railroads to improve the communications flow to shippers on rate changes. The Southern Freight Association is implementing a system of electronic data interchange. We submit that the railroads should be responsible to make certain that shippers have adequate notice of rate changes. I am hopeful that the railroads will accept and accomplish this responsibility. The change to 10 and 20 days can be beneficial to railroads and shippers alike, however, without shippers knowing their transportation costs at time of shipment, grain marketing will be adversely affected.

I would like to summarize the following points:

1. It is too early to assess the long-range effect of the Staggers Act.
2. There must be full disclosure of all contract provisions on agricultural commodities.
3. While the Staggers Act prohibited publication of demand-sensitive rates on agricultural commodities, the intent of Congress is not being followed.
4. Railroads need to assume the responsibility of advising shippers of rate changes in a timely manner.

Senator DANFORTH. Thank you, Mr. Stepner. Mr. Zitto?

Mr. ZITTO. Senator, my name is Fred Zitto, manager of the U.S. distribution operations of International Paper Co. I'm appearing for American Paper Institute. With me is John F. Donelan, transportation counsel for API. I appreciate the opportunity to comment briefly at this time. I would like to emphasize three points, two of them involving action by the Interstate Commerce Commission, and a third involving what we regard as a necessary amendment to the contract provisions of the Staggers Rail Act.

API supports the economic deregulation of railroads, providing necessary protection is maintained for shippers faced with railroad monopolies, that is, market dominance. This protection is a great counterbalancing force in both the 4R Act and the Staggers Rail Act. The standards for the determination of market dominance set by the Commission pursuant to the 4R Act were upheld by the U.S. Court of Appeals for the District of Columbia. The essential defini-

tion of market dominance in the 4R Act was not changed by the Staggers Rail Act.

Now with no mandate from Congress whatsoever, the Commission has thrown out the prior rules and leaves the determination of market dominance to a case-by-case basis. Indeed, the injection of the new criterion of product competition will, if tolerated, destroy the protection for railroad market dominance and will result in far more economic deregulation than Congress ever contemplated.

Insofar as the paper industry is concerned, the use of product competition could well result in virtual deregulation of rail transportation of our shipments.

API supports the new provisions of the Staggers Rail Act pertaining to railroad transportation contracts, again given appropriate protection to the shipping public. However, the present provisions have actually acted to obstruct the entering of railroad transportation contracts by members of the paper industry. API is offering an amendment to section 10713, subsection (k)(1). We would emphasize that this amendment does not affect provisions governing agricultural and forest product commodities generally. It is limited solely to the paper industry, in that it excludes from subsection (k)(1), paper, wood pulp, wood chips, or pulpwood.

This provision would not affect overall provisions maintaining the railroad's common carrier obligation, a ban against unreasonable discrimination, and the prohibition against predatory practices.

We are unable to find any justification whatsoever or need by the paper industry for the two 40 percent limitations which are presently contained in section 10713 of the act.

Under section 203 of the Staggers Rail Act, the Commission is charged with developing at least on a quarterly basis a cost index to reflect true increases in the costs incurred by the railroads. Clearly, the Congress was interested in compensation for true increases in cost. In implementing these provisions, the Commission has committed serious errors. No. 1, the Commission is relying solely on railroad-furnished data with no input from shippers. No. 2, the Commission has blatantly disregarded the impact of improved railroad productivity in determining the cost index by utilizing price data rather than cost data. An independent economic analyst retained by API has noted that the AAR input price index historically has radically overstated actual cost increases.

I would like to complete this short statement by one overall point of principle. Our industry is deeply concerned that the Commission's implementation of the Staggers Rail Act seriously fails to preserve the protections for the shipping public which Congress intentionally provided.

Thank you.

[The statement follows:]

STATEMENT OF FRED M. ZITTO ON BEHALF OF THE AMERICAN PAPER INSTITUTE

My name is Fred M. Zitto. I am Manager, U.S. Distribution Operations of International Paper Company. My business address is 77 West 45th Street, New York, NY 10036. I appear for American Paper Institute, Inc., to whom I shall sometimes refer as API. With me is Mr. John F. Donelan, who is Transportation Counsel for API. Mr. Donelan's business address is Washington Building, Washington, D.C. 20005.

I have been actively engaged in the field of transportation and distribution for approximately 28 years. My present duties with International Paper Company include responsibility for management of all transportation for my company within the United States via rail and all other modes.

API is the national trade association of the pulp, paper and paperboard industry and consists of approximately 175 manufacturers which produce approximately 90 percent of the nation's output of these products. The primary industry, including its converting segments, which operates in all states of the Union, employs approximately 700,000 people. Our industry relies very heavily on rail transportation for both its inbound and outbound materials and products.

API welcomes the opportunity to participate in these oversight hearings. API played a very active role in the hearings which ultimately led to the enactment of the Staggers Rail Act. The same is true with respect to the 4-R Act. API has participated actively in the various rulemaking proceedings before the Interstate Commerce Commission, implementing the provisions of the new law. It is out of that experience and the day-to-day business observations in the field of transportation and distribution that API presents these points today.

I.C.C. FAILURE TO DEVELOP FULL RECORDS IN IMPLEMENTATION PROCEEDINGS

API has noted a serious defect in practically every one of the rulemaking proceedings under the Staggers Rail Act (which I shall sometimes call SRA). The I.C.C. made no provisions whatsoever for the issuance of a service list of parties or for providing parties the opportunity of responding to the filings of others in the case. The result was that the records lacked the healthy balance which arises when representations by individuals are subjected to review, analysis and comment by other knowledgeable persons.

It was API's experience that it was only with great difficulty one could even learn who was participating in these proceedings, let alone obtain copies of their representations.

Inconsequence the I.C.C. lost extremely valuable input which would have contributed to sound and valid conclusions. API is aware that time was important. However API has no doubt that these deficiencies could have been remedied and the time frames could have been preserved.

Respectfully API urges the Congress to direct the Commission in the future in these types of rulemaking proceedings to provide for the counterbalancing input we have mentioned above.

I.C.C. FAILURE TO PERMIT FULL SHIPPER PARTICIPATION IN IMPLEMENTING STAGGERS RAIL ACT

In its testimony in support of the Staggers Rail Act and the 4-R Act, as well, API indicated its strong support of the concept of economic deregulation so far as possible. In instances where shippers faced railroad monopoly power API supported protection for such shippers.

In taking these positions API also supports the goal of SRA that where the regulatory process continues to operate it should balance the interests of the carriers, the shippers and the public.

API feels that while the Commission may give lip service to the participating role of the shipper in practice the I.C.C. is falling well short of the mark. A case in point is the matter of the railroad cost recovery index contemplated in the SRA to enable the railroads to offset increases in costs when the same have occurred. This subject has been covered in I.C.C. Docket Ex Parte No. 290 (Sub-No. 2). API has challenged and continues to challenge (1) the reliance of the Commission on cost data provided totally by the railroads; (2) I.C.C. failure to discount such data as required by economic realities; and (3) I.C.C. exclusion of the shippers from the ultimate process whereby the data are utilized to produce the railroad cost recovery index which the the railroads are allowed to use to put rate increases in effect on one day's notice.

When utilized this railroad cost recovery index can add billions of dollars to the nation's transportation burden. The letter and the spirit of the Staggers Rail Act require that the errors API has cited above be immediately corrected. Particularly, there must be provision for full participation by the shippers in the process from beginning to end.

RADICAL DEPARTURE OF I.C.C. FROM PRIOR PRINCIPLES, WITH NO BASIS FOR SUCH ACTION IN SRA

We repeat again the ultimate aim for economic deregulation supported by API. We are here talking about the area where regulation continues, in accordance with

the will of the Congress. One important area covered both in the 4-R Act and SRA is the determination of adequacy of revenues for the railroads.

This has been the subject of several proceedings by the Commission in which API has been, beyond question, one of the most active parties. Principles were enunciated, based on extensive records in Ex Parte Nos. 338, 353, 363 and 381.

Suddenly, in Ex Parte No. 393 the I.C.C., during the era of Chairman Gaskins, reversed its course, applied a wholly new standard on cost of capital. The result of this was to reverse earlier findings and designate practically all the test railroads as allegedly suffering from revenue inadequacy. We refer to such railroads as the Burlington Northern, the Union Pacific, the Chessie System, the Southern Railway System—and several others. It is API's view that this result is seriously in error.

In our view, the Staggers Rail Act can be searched from beginning to end and there is absolutely no warrant for this kind of radical reverse of course taken by the I.C.C. in this instance. This is grossly unfair and injurious to the shipping public and has no warrant under the Staggers Rail Act.

COMMISSION HANDLING OF SURCHARGE PROVISIONS OF SECTION 217 OF THE STAGGERS RAIL ACT

In its testimony in the hearings preceding the Staggers Rail Act API supported both the concept of economic deregulation and the need for healthy railroads to provide transportation service to the shipping public. API made specific contributions to the discussion and analysis which led to the enactment of § 217 of SRA. API has actively participated in Ex Parte No. 389, the rulemaking proceeding to implement these statutory provisions.

While progress has been made in enabling shippers to obtain the cost and revenue determination, API has been disturbed by the failure of the Commission to prevent railroads from employing the § 217 provisions on a blanket or territorial basis as distinct from a selective basis. API does not read the statutory provisions as permitting this kind of across-the-board approach taken by the railroads, particularly Conrail.

API also objects to the provision by the I.C.C. in implementing these provisons that tariff minimum weights will be used instead of actual minimum weights. Actual minimum weights reflect the factual situation. In API's view the use of the tariff minimum weights is seriously injuring the shippers in terms of implementing the surcharge provisions.

Section 217 had as its purpose to see that railroads such as Conrail were made whole not that they were to receive an artificial "windfall" through this particular surcharge mechanism.

I.C.C.'S UNJUSTIFIED WEAKENING OF THE BROAD TARIFF EXEMPTION IN THE RATE BUREAU PROVISIONS

In its testimony supporting, so far as possible, economic deregulation API specifically noted the nature of the pulp, paper and paperboard industry. The products of our industry move literally into every hamlet, village, town, city, county of this nation. Over the years, in consequence, the railroads have published broad tariff adjustments, including intraregional and interterritorial rate scales to facilitate the movement of these products. In recognition of this API in testifying requested the Congress to continue the broad tariff exemption which had also been enacted in the 4-R Act, to meet this need until an appropriate substitute could be found.

It was our understanding that this matter had been taken care of under the Staggers Rail Act. However, the Interstate Commerce Commission has seen fit in large measure to cripple the broad tariff exemption by prohibiting the rate bureaus from embracing single line rates under such broad tariff exemption. This occurred even though API had placed in the record substantial evidence as to the need to include single line rates within the broad tariff exemption.

This action by the Commission, over the objection both of the railroads and the shippers, has undermined and is undermining the broad tariff exemption.

Turning to § 219 of the Staggers Rail Act and more specifically Title 49 U.S.C. § 10706(a)(3)(B)(ii) the exception should be deleted and subsection (ii) should read, without exception: "broad tariff changes that are of at least substantially general application throughout the area where the changes will apply."

If this is done then our industry will have received what it expected to receive and which will enable us to continue to function effectively at least until January 1, 1984.

The vice to which we object is two-fold: first, it is artificial and unrealistic to try to segregate from these broad tariff adjustments those which apply in single line

movements only. Secondly, we sense that with the present statutory exception the railroads are reluctant even to promulgate joint line rates for fear of charges of antitrust violations when subsequently, for indisputably competitive reasons, individual carriers publish the same rates on a single line basis.

IMPROPER AND UNWARRANTED NARROWING OF THE MARKET DOMINANCE PROTECTION FOR SHIPPERS

While API has supported economic deregulation, where the competitive forces of the marketplace protect shippers, API has recognized that there is a significant area where the shippers face railroad monopoly, referred to in the Staggers Rail Act and the 4-R Act as railroad market dominance. Pursuant to the 4-R Act, the Commission in Ex Parte No. 320 establish standards for the determination of railroad market dominance. These standards were upheld on review by the U.S. Court of Appeals for the District of Columbia Circuit. The approach taken by the Commission was to establish certain rebuttable presumptions indicating railroad market dominance, subject to proof to the contrary by the railroads.

The Staggers Rail Act did not change the definition of market dominance in the 4-R Act as follows: ". . . an absence of effective competition from other carriers or modes of transportation, for the traffic or movement to which a rate applies . . ." (4-R Act, § 202(b)).

The Interstate Commerce Commission has recently issued its decision in Ex Parte No. 320 (Sub-No. 2) and has drastically changed the methodology to be employed in determining railroad market dominance. The I.C.C. has scrapped the rebuttable presumptions. Beyond that it has seen fit to inject two essentially new concepts in this sphere: product competition and source competition.

The result is to turn the issue of the determination of market dominance into a complex maze, if not fiasco, to the serious injury of captive shippers.

In API's view there is no warrant for such drastic action in the Staggers Rail Act and, indeed, in our judgment it is contrary to specific provisions of the Staggers Rail Act. (See § 205 of SRA)

It is impossible to overstate the importance of this. In API's view while Congress conferred freedom in large areas upon the railroads, Congress was vigilant to protect shippers who did not have the benefit of effective competition. There is the strongest public and Congressional policy behind insuring that the statutory protection of captive shippers is preserved. In its latest decision the I.C.C. has moved sharply toward the dilution of this vital protection to captive shippers. Congress should make clear that the vitality of the market dominance provisions is to be preserved and not to be undermined as was done when the Commission saw fit, in its most recent decision, to inject the irrelevant concepts of product and source competition.

I.C.C. FAILURE TO INSURE ADEQUATE RAIL CAR SUPPLY

Our industry is one of the key industries of the nation and it is one of the leading customers of the railroads. The corollary of this is that we are dependent upon the railroads for transportation service.

In approaching the Staggers Rail Act in our testimony API stressed the importance of the fact that the Commission must ultimately retain and exercise its car service powers to insure the proper functioning of the national railroad network.

One the key Commission proceedings has been Ex Parte No. 241, the *Railroad Car Supply Investigation.* There originally the Commission had provided for mandatory car service rules, the first two of which required that railroad cars when empty be returned to their owners. This is of extreme importance to our industry which requires cars for the movement of our raw materials from the woodlands areas which are often on the periphery of the nation's rail systems.

API was astonished and distressed when the Commission reversed its earlier directives in Ex Parte No. 241 and cancelled mandatory Car Service Rules 1 and 2 last year.

One must take the long view with respect to railroad car supply because we have had a long history from which to learn. At this precise time there is an abundance of rail cars so that this change currently may present no problem. However, past is prologue. The times will come again when there will be shortages of cars and the absence of mandatory Car Service Rules 1 and 2 will cause our industry grave injury. Neither the I.C.C. nor the railroads have made any provision for the future to meet this inevitable eventuality through the substitution of another system. Until this is done these car service rules should be reinstated on a mandatory basis. This cannot be left to chance or happenstance.

This subject was clearly in the minds of the Congress. Then Chairman Cannon, in debating the bill in the Congressional Record on April 1, 1980 stated:

"Mr. CANNON. Mr. President, I understand some shipping interests have expressed concern as to the scope of section 301 of S. 1946 as to car service. An important distinction must be borne in mind. Section 11123 of title 49 is being amended as to the required regional or national type emergency before the Interstate Commerce Commission can issue car service orders, as well as the duration and the scope of the car service orders.

"I want to emphasize that the provisions of section 11122 of title 49 of the United States Code as to permanent rules and regulations on railroad car service are unaffected and remain intact. We must remember the importance of insuring on a day-to-day basis the efficient functioning of our unified national rail system and network. The Commission still retains its power to issue permanent mandatory car service rules such as those which are now in effect and which govern the movement of railroad cars throughout the country."

This concern was also expressed in the Conference Report on the Staggers Rail Act of 1980, No. 96-1430 at p. 119 as follows:

"The Conferees want to emphasize that the provisions of section 11122 of title 49 of the United States Code as to permanent rules and regulations on railroad car service are unaffected and remain intact. The importance of insuring on a day-to-day basis the efficient functioning of our unified national rail system and network remains. The Commission still retains its power to issue permanent mandatory car service rules such as those which are now in effect and which govern the movement of railroad cars throughout the country."

One of the goals of SRA is a regulatory process that balances the needs of the carriers, the shippers and the public. In this regard our industry insists that we are entitled to insurance of adequate car supply through the reinstatement of Car Service Rules 1 and 2 on a mandatory basis.

CHANGES REQUIRED IN SUBSECTION (K) OF 49 U.S. CODE SECTION 10713, PERTAINING TO CONTRACTS, IN ORDER TO AVOID UNWARRANTED AND SUBSTANTIAL INJURY TO THE PAPER INDUSTRY

One of the significant changes brought about by the Staggers Rail Act is Section 208 pertaining to Contracts now found in 49 U.S.C. Code § 10713. Much that is in this Section is sound and has the support of API. However, in Subsection (k)(1) of § 10713, there appear two so-called "40 percent" limitations, indicated in the statutory language quoted below:

"(k)(1) Any rail carrier may, in accordance with the terms of this section, enter into contracts for the transportation of agricultural commodities (including forest products and paper) involving the utilization of carrier owned or leased equipment not in excess of *40 percent* of the capacity of such carrier's owned or leased equipment by major car type (plain boxcars, covered hopper cars, gondolas and open top hoppers, coal cars, bulkhead flatcars, pulpwood rackcars and flatbed equipment, including TOFC/COFC), except that in the case of a proposed contract between a class I carrier and a shipper originating an average of 1,000 cars or more per year during the prior 3-year period by major car type on a particular carrier, not more than *40 percent* of carrier owned or leased equipment utilized on the average during the prior 3-year period may be used for such contract without prior authorization by the Commission." (Emphasis added)

These limitations are causing harassment and injury to the paper industry as it seeks to utilize the contract provisions of Section 208 of the Staggers Rail Act. We see no reason or justification for these limitations with respect to the railroad equipment utilized by our industry, namely, boxcars, pulpwood rackcars and wood chip cars.

We would emphasize that all members of our industry who use these cars have the protection contained in Section 10713 in terms of the railroads remaining able to meet their common carrier obligations. API supports this. In the sphere of agricultural commodities (including forest products and paper), all our members have the benefit of the protective provisions against unreasonable discrimination and the protective provisions prohibiting destructive competitive practices. All our members have the protection of the federal antitrust laws pertaining to contracts under Section 10713.

The simple fact is that the application of the two 40 percent limitations of Subsection (k)(1) is obstructing if not preventing effective use of the Staggers Rail Act contract provisions by the paper industry.

To us, the remedy is simple. It is to exclude from the application of Subsection (k)(1) *only* coverage of paper and within the broad category of forest products,

coverage of pulpwood, wood chips and woodpulp. We are here dealing with matters which we feel are of concern solely to the paper industry. The Appendix attached to this Statement contains language which would remedy this problem.

Our own investigation to date has revealed no justification for the present language in the statute which we have been discussing. Our industry has simply not been able to find any justification for the 40 percent limitations which we have discussed. This is particularly so in the light of the other important provisions which protect the paper shipper—the obligation to meet the common carrier duties, the ban against unlawful discrimination and the ban against predatory practices. In a word, we feel that the Appendix does the job. We thank you for the opportunity to present our views.

APPENDIX

CONTRACTS

SEC. . Section 10713(k)(1) of title 49, United States Code, is amended to read as follows:

"(k)(1) Any rail carrier may, in accordance with the terms of this section, enter into contracts for the transportation of agricultural commodities [including forest products and paper] *(including forest products generally but, as to subparagraph (k)(1) only, not including paper, wood pulp, wood chips, or pulpwood)* involving the utilization of carrier owned or leased equipment not in excess of 40 percent of the capacity of such carrier's owned or leased equipment by major car type (plain boxcars, covered hopper cars, gondolas and open top hoppers, coal cars, bulkhead flatcars, pulpwood rackcars, and flatbed equipment, including TOFC/COFC), except that in the case of a proposed contract between a class I carrier and a shipper originating an average of 1000 cars or more per year during the prior 3-year period by major car type on a particular carrier, not more than 40 percent of carrier owned or leased equipment utilized on the average during the prior 3-year period may be used for such contract without prior authorization by the Commission."

Senator DANFORTH. Thank you, gentlemen.

Let me again say to each witness that your entire statement will be included in the record. Also the record will be kept open for an additional 30 days to receive statements that anyone cares to submit.

Also there may be written questions for some of the witnesses. I know Senator Riegle indicated that he had questions for one of the witnesses. So some witnesses will be receiving questions from committee members. The record will also be kept open for that purpose.

[Whereupon, at 11:25 a.m., the hearing was adjourned.]

ADDITIONAL ARTICLES, LETTERS, AND STATEMENTS

Statement of American Iron & Steel Institute

This statement is submitted by the American Iron and Steel Institute (AISI) to the United States Senate, Committee on Commerce, Science, and Transportation, Subcommittee on Surface Transportation for inclusion in the record of the Oversight Hearing on Staggers Rail Act of 1980.

The AISI is a trade association representing foreign and domestic steel companies, including 66 domestic member companies which collectively account for approximately 91 percent of the raw steel production in this country. Due to the nature of the iron and steel industry, its products and shipping practices, AISI members require reliable rail service. It has been estimated that it takes approximately three tons of raw material to make one ton of finished steel product. Raw materials such as coal, coke, limestone, and iron ore move to AISI member plants by rail.

These comments are directed to four subjects which are of concern to AISI members: (1) Market Dominance Guidelines; (2) Railroad Cost Recovery Procedures; (3) National Coal Rate Guidelines; and (4) Pre-Staggers Act Contracts.

All of these subjects are complex and presently in litigation before the Interstate Commerce Commission and/or the courts. The thrust of the AISI position on each subject is that the Interstate Commerce Commission's implementation of the Staggers Act is not in conformity with the Congressional intent.

1. *Market Dominance.*—The I.C.C.'s adoption of "evidentiary guidelines" relating to product and geographic competition is not authorized by the 4R Act or the Staggers Act.

In railroad rate matters, a finding of market dominance is necessary to establish the jurisdictional threshold for I.C.C. consideration. In the Ex Parte 320 proceedings, I.C.C. holdings relative to the definition of market dominance have been inconsistent and ambiguous. Previous rules regarding rebuttable presumptions have been abandoned. Product competition and geographic competition are factors which the I.C.C. now proposes to consider in connection with the jurisdictional threshold of market dominance, despite its previous rejection of such factors as inconsistent with Congressional intent.

The I.C.C. has authority to determine maximum reasonable rail rates only where the railroads have "market dominance." This term was introduced and defined in the 4R Act as an "absence of effective competition from other carriers or modes of transportation for the transportation to which a rate applies." Congress made no change in this definition in the Staggers Rail Act of 1980.

In the 4R Act, Congress directed the Commission to "establish by rule, standards and procedures for determining," whether a railroad possesses market dominance. Congress further provided that these standards and procedures must be "designed to provide for a practical determination without administrative delay." 4R Act Section 202(b), Pub. L. 94-210, 90 Stat. 31, 35 (1976).

The Commission promptly complied with this requirement by issuing rules for market dominance determinations. These rules focused solely on direct competition by other rail carriers or other carrier modes (e.g., motor or barge) for traffic between a given origin and destination. During this rulemaking, the railroads urged the Commission to consider indirect competition as well, including "product" competition (the availability of a substitute commodity) and "geographic" competition (the ability of the shipper to obtain the same or a substitute commodity from different origins or to receive it at different destinations.) The Commission flatly rejected the concepts of product and geographic competition as incompatible with express language of the 4R Act market dominance definition and the 4R Act's requirement of administrative practicality. The Commission met these requirements by establishing rebuttable presumptions of market dominance based entirely on direct competition for the traffic at issue in any given case. See Ex Parte No. 320, Special Procedures for Making Findings of Market Dominance as Required by the Railroad Revitaliza-

tion and Regulatory Reform Act of 1976, Interim Report, 353 I.C.C. 875 (1976) (Interim Report).[1]

The Commission's rules were affirmed by the United States Court of Appeals and were applied by the Commission in hundreds of cases between 1976 and 1980.

After passage of the Staggers Act, the Commission issued a "Notice of Proposed Policy," seeking comments as to whether it should eliminate the market dominance presumptions it had established. After receiving comments, the Commission on July 8, 1981, issued a decision in which it abandoned the rebuttable presumptions, reversed its interpretation of the statute on the question of geographic and product competition, and revoked its position on the weight to be given rail-related investments and long-term supply contracts. In place of the presumptions the I.C.C. listed over thirty evidentiary "guidelines" that it may use in any given market dominance determination. The I.C.C.'s guidelines, while "not exhaustive," generally assign no weight or relative value to the types of evidence listed, but give full weight to suggestions of geographic and product competition made by railroads and little or no weight to evidence of rail-related investments made, and long-term supply contracts entered into, by shippers after October 1, 1980, the effective date of the Staggers Act. In its July 8 decision, the Commission also decided, without prior notice or opportunity for comment, to place on shippers the burden of proving that product or geographic competitions suggested by the railroads in particular cases are not effective restraints upon railroad pricing. Ex Parte No. 320 (Sub. No. 2), Market Dominance Determinations and Consideration of Product Competition, 365 I.C.C. 118, 132–135 (1981).

The I.C.C.'s new evidentiary guidelines can cause severe problems for the steel industry. For example, consider a steel company which makes a substantial investment in a metallurgical coal mine to assure a long term supply of a very special type of coal needed to produce coke used in blast furnaces. Coal of a certain quality is essential to the operations—not just any coal will do. The mine is served by only one railroad, which is quite common at steel company coal mines. If the rate of moving the coal from the mine to the destination steel plant is challenged, the railroad can simply assert that product and geographic competition exist, and the steel company, in a very limited amount of time, normally less that 10 days, has the burden of trying to prove that buying other coal at other locations, possibly moving by other modes, is not a practical alternative.

Decisions regarding raw material specifications involve extremely technical issues which are often intensely debated within companies and among industry experts. Manifestly, the I.C.C. is not qualified to measure the economic penalties associated with the use of alternative coals, if indeed they could be found in the quantities required, nor does it have the expertise to evaluate the costs associated with quality and/or productivity problems likely to be encountered in subsequent operations by the use of alternate coals. It is the concern over these problems that compels a steel company to invest in metallurgical coal mines in the first place. A shipper forced to use an alternative source of coal because of high rates, found not subject to I.C.C. jurisdiction, may find himself in a similar position with respect to the level of rates from the new source. In the example cited, the only railroad serving the mine has, by any reasonable definition, market dominance over the movement of coal to the steel plant. Under the new rules, the railroad would argue that the traffic is not market dominant because other coals are available from other origins which could possibly move by other modes. Under the new rules, also, little or no weight would be given to a long-term coal supply contract, or to substantial investment in a mine, or to investment in rail related facilities at the origin and destination plant. Circumstances described in the example of coal apply equally to iron ore. At the very least, the railroad should be required to make a *prima facie* showing of the existence of product and geographic competition. Instead, under the I.C.C.'s new guidelines, the railroad need only identify where it "believes" such competition may exist, and the burden of proof shifts to the shipper.

[1] In the Interim Report, the Commission established that a rebuttable presumption of market dominance would arise on a showing of any one of the following fact situations: (1) the rail carrier handled 70 percent or more of the involved traffic or movement during the preceding year; (2) the rate at issue exceeded the variable cost of providing the service by 60 percent or more; or (3) shippers or consignees had made a substantial investment in rail-related equipment or facilities which prevented or made impractical the use of another carrier or mode. The Commission's rule also provided that, if the rate in issue had been discussed under a rate bureau agreement filed with the Commission, a rebuttable presumption would arise that a carrier participating in the rate or discussion does not provide effective competition to the proponent rail carrier for the involved traffic. 49 C.F.R. Section 1109.1 (1980).

The shipping community, including the steel industry, has been sympathetic to the financial plight of the railroads and generally supported the Staggers Act rate flexibility provisions with the understanding that there would be adequate protection for traffic that is captive to rail. The protection captive shippers had is steadily being eroded by I.C.C. decisions since the Staggers Act became law.

AISI POSITION

The I.C.C.'s adoption in Ex Parte No. 320 of "evidentiary guidelines" relating to product and geographic competition is not authorized by the 4R Act or the Staggers Act. This is conclusively demonstrated by both the language and the legislative history of the statutes. In issuing this decision, the Commission has stepped well outside the bounds of its statutory authority.

The Commission originally interpreted the 4R Act's definition of market dominance to exclude consideration of product and geographic competition. This reading of the 4R Act was made contemporaneously with the passage of the statute and was confirmed on appeal.

The I.C.C. tries to justify its dramatic reversal by resorting to the Staggers Act. The Staggers Act, however, provides no support for the Commission's action. The Staggers Act left the definition of "market dominance" intact. In fact, the legislative history of the Staggers Act demonstrates that Congress confronted, debated, and eventually discarded any notion of injecting product and geographic competition in market dominance proceedings.

In addition, the Commission makes no attempt to explain how implementation of the new guidelines will permit "practical determinations" of market dominance "without administrative delay" within the statutorily mandated, ninety-day time period. The I.C.C. initially relied on the same statutory requirements when it interpreted Congress' market dominance definition to preclude consideration of product and geographic competition. The I.C.C. was correct. Such considerations are inconsistent with the rapidity requirement of the 4R Act, and the I.C.C. in its July 8 decision comes forward with no explanation to justify any other conclusion.

By altering the product and geographic competition rules, the Commission further errs in assigning itself expertise in many areas beyond its competence. Although the Commission was set up by Congress to exercise its expertise in the area of transportation regulation, the implementation of the new guidelines will require the Commission to decide the complex economic, engineering, and manufacturing issues which will arise in market dominance inquiries. This venture by the Commission into new areas far afield of the agency's traditional domain was never contemplated by Congress.

Even if considerations of product and geographic competition were permissible, the Commission further exceeds its authority and contravenes Congressional intent by allocating to shippers the burden of proving a negative—the absence of product and geographic competition. This new evidentiary rule was issued without prior notice. Moreover, the allocation of this burden, which is irrationally based on an unsupported presumption of the existence of market dominance in every case, is squarely contradicted by the statute and its legislative history.

The I.C.C.'s decision to give little or no weight to evidence of substantial rail-related investments and long-term supply contracts in market dominance determinations further subverts Congressional intent. The Commission asserts that the enactment of Section 208 of the Staggers Act, which permits shippers and carriers to contract for transportation services, dictates that such evidence by given little weight. It does nothing of the sort. Section 208 is completely irrelevant to market dominance proceedings. Market dominance is in issue only when a contract is not involved.

Congress enacted Section 208 to encourage voluntary contracting by shippers and carriers. The I.C.C.'s guidelines, however, penalize shippers who cannot reach agreements with the railroads, eviscerate a captive shipper's statutory protection from unreasonable rates, and discourage shipper investment in rail-related facilities, all contrary to the express intent of Congress.

2. *Railroad Cost Recovery Procedures.* The I.C.C.'s adoption of the AAR Index is contrary to the intent of the Staggers Act.

In a decision issued on April 17, 1981, Ex Parte 290 (Sub No. 2), the I.C.C. adopted rules implementing Section 203 of the Staggers Act which permits railroad rates to be increased on an individual basis four times a year, by the percentage increase in an index of railroad costs to be compiled or verified by the Commission.

The Commission elected not to compile its own index, but instead, to use the Index of Railroad Material Prices and Wage Rates—the so-called AAR index—complied by the Association of American Railroads. The AAR Index is a weighted

index of the prices the railroads pay for purchased materials, and the wage rates they pay their employees. The AAR Index is supplemented by the Producers' Price Index as a temporary surrogate for inputs not yet covered by the AAR Index.

The AAR Index is now used to recover inflationary cost increases and affects virtually all of the published base rates. Such increases are totally immune from challenge. The use of an index that accurately reflects increases in costs is important because even a slight overstatement of cost translates into a substantial number of dollars.

AISI POSITION

The basic shortcoming of the AAR Index is that it provides unlimited opportunity to pass through higher prices. No incentive exists to keep prices, covered by the index, under control. Higher prices simply trigger higher rates. The index, in effect, nurtures inefficiency.

Moreover, utilizing an index which is maintained by the AAR as a determinant of rail rates raises serious questions as to the impartiality of the index. I.C.C. Chairman Taylor recently called attention to two problems resulting from a retroactive adjustment which AAR made in the index, as follows:

"A question of consistency arises if overestimates are to be corrected by the index's self-adjusting mechanism while underestimates are to be corrected by retroactive adjustment additives.

"The second and, in my opinion, more serious problem arises from the fact that the wage increases reflected in the AAR's Third Quarter Index (and perhaps in subsequent indices) have not been disbursed. The railroads have enjoyed the use of a very substantial revenue increase for which no corresponding disbursement has been made." [2]

The use of the AAR Index is also inappropriate because it does not properly reflect cost increases as required by the Staggers Act. The AAR Index is an index of prices not costs and, as a result, does not reflect increases in labor productivity or efficiency in the utilization of materials which are accomplished. Nor does the AAR Index reflect the economics of scale resulting from an expanding volume of traffic.

The use of the AAR Index assumes that all traffic uses the same mix of labor and materials. Use of the index is particularly inappropriate for escalating unit train and train load rates on such commodities as coal and iron ore where service provided under such rates contains much less labor, plant, and equipment per unit than does average traffic.

The use of the AAR Index is incompatible with the intent of Congress as expressed in section 203 of the Staggers Act and adjusting rates by use of the AAR Index will result in increases in rates which greatly exceed increases in cost.

Coal Rate Guidelines—Nationwide. The I.C.C.'s proposed adoption of the ton/ton mile method of allocating costs deprives shippers of coal and ore of the maximum rate protection required by the Staggers Act.

The I.C.C., in a proceeding known as Ex Parte No. 347 (Sub. No. 1) Coal Rate Guidelines—Nationwide, proposes to implement new coal rate guidelines which would change the method of allocating fixed or constant costs from the ratio of revenue method, which it had consistently employed for several years, to a ton/ton mile approach. The result of this change is to place selectively a disproportionately high share of the fixed costs on heavy-loading, high-volume commodities such as coal and iron ore which are predominantly captive to rail.

The ton/ton mile method divides constant costs into those associated with terminal and those associated with line-haul services. Terminal costs are allocated solely on the basis of tons; line-haul services are allocated using a combination of tons times distance carried (ton miles). The ton/ton mile method totally ignores the economic efficiencies characteristic of most heavy-loading bulk commodities which move in repetitive trainload or unit-train service. The distortion is particularly acute at the terminal level, because shippers and carriers of large-volume traffic such as coal and iron ore, by avoiding to a very substantial extent all terminal costs, have made operations many times more efficient than is normally possible with single car traffic. Moreover, this distortion becomes more onerous as the length of haul decreases, because of the increased percentage of total costs allocable as terminal constant costs.[3]

The Commission's purpose in now proposing the adoption of the ton/ton mile method is to allocate to heavy-loading trainload or unit train traffic a disproportion-

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[2] Ex Parte 290 (Sub No. 2) separate expression of Chairman Taylor, Oct. 5, 1981.

[3] The iron and steel industry shipped in excess of 50 million tons of iron ore by rail in 1980; the length of haul for approximately 90 percent of that tonnage was less than 130 miles.

ate share of total system constant costs solely because such traffic is captive and therefore has no competitive transportation practically available to temper the exercise of market power by the railroads. This is action which the Staggers Rail Act sought to preclude and, in reality, constitutes nothing more than an attempt to resuscitate the Commission's admittedly imprecise "7 percent solution," which has been uniformly struck down as arbitrary and capricious by the Court of Appeals. By comparison, the ton/ton mile burden which the Commission seeks to visit on captive volume rail users is even more onerous than a 7 percent solution, particularly on short-haul traffic.

Although the Commission has not yet finally adopted the ton/ton mile method in Ex Parte 347, it has begun to apply the method in individual coal rate cases. In an appeal of such a decision filed by a utility company shipper, the Department of Justice attacked the Commission's use of the ton/ton mile method as vigorously as it attacked the "7 percent solution." In every case, the Justice Department has criticized the Commission's explanation of its use of the "7 percent solution" and the ton/ton mile method as totally inadequate and has refused to defend it.

AISI POSITION

AISI opposes the adoption of such guidelines as the ton/ton mile method of allocating costs because it discriminates against heavy loading, short haul traffic and arbitrarily places the greatest share of fixed costs on traffic having the greatest cost efficiencies in order to subsidize rail traffic for which there is substantial intermodal competition. AISI believes it is contrary to the Staggers Act for the Commission to adopt a standard requiring that traffic such as coal and iron ore subsidize other traffic. Such a standard would deprive users of coal and ore of the maximum rate protection required by the Long-Cannon amendment, Section 203 of the Staggers Act, now 49 U.S.C. Section 10707a(e)(2)(C), and the Staggers Act amendments to the National Transportation Policy.

4. *Pre-Staggers Act Contracts.* The I.C.C.'s contention that it has jurisdiction over pre-Staggers Act contracts is not consonant with Congressional intent.

Section 208 of the Staggers Rail Act authorizes railroads and shippers to enter into contracts governing the rates and services on particular movements. Once approved, the exclusive remedy for any alleged breach of a contract entered into shall be an action in an appropriate State Court or United States District Court. Congress, for the first time, has divested the I.C.C. of a portion of its previously exclusive jurisdiction over rail rates and expressly given jurisdiction over rate contracts to the courts.

The I.C.C., however, while admitting its lack of jurisdiction over rate contracts entered into after the effective date of the Staggers Act, contends that Congress has not divested it of jurisdiction over contracts entered into before the Staggers Act. The I.C.C. ignores the language of Section 208(j), the grandfather provision, which provides that any lawful pre-Staggers Act contract "shall hereafter have the same force and effect as if it had been entered into in accordance with the provisions of this section."

A clear indication of Congressional intent can be found in the floor remarks of Congressman Dingell who sponsored this provision:

"New Section 19713 provides for the entry and enforcement of rate contracts between shippers and railroads. Sub-section (j) thereof includes my suggested language preserving rights arising out of existing contracts. Indeed, the second sentence of sub-section (j) provides that existing contracts shall have the same force and effect as if they had been entered into in accordance with other provisions of Section 19713. This insures not only that the legislation leaves existing contracts untouched, but also that such contracts will enjoy the same newly created enforcement rights established for contracts entered into after its passage." [4]

Since the effective date of the Staggers Act, three courts have considered the issue of jurisdiction over pre-Staggers Act contracts. In each case, the courts held that they have jurisdiction to enforce lawful pre-Staggers Act contracts. *The Cleveland-Cliffs Iron Co., et al.* v. *Interstate Commerce Commission, et al.*, Nos. 79-3775, et al. (Sixth Circuit, decided November 20, 1981.) *Metallurg, Inc.* v. *Burlington Northern, Inc.* No. 3-81 Cir. 39 (D. Minn. April 10, 1981.) *The Cleveland-Cliffs Iron Co.* v. *Chicago & Northwestern Transportation Co.*, 516 F.Supp. 399 W.D. Mich. 1981.

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[4] 126 Congressional Record H10085 (daily ed. Sept. 30, 1980)

AISI POSITION

The I.C.C.'s contention that it has jurisdiction over pre-Staggers Act contracts is not consonant with Congressional intent as expressed in Section 208(j) of the Staggers Act and the Act's amendments to the National Transportation Policy to allow free market forces, and not the regulatory process, to set rates. AISI believes that the Congressional intent was to place jurisdiction over lawful pre-Staggers Act contracts with the courts, just as they have with post Staggers Act contracts.

CONCLUSION

The I.C.C.'s record on the four issues discussed above is not commendable. The Commission has thwarted Congressional intent expressed in the Staggers Act on the critically important issues of market dominance, inflation-based cost recovery, jurisdiction over rail contracts, and maximum reasonable rate guidelines. The Commission's action on the first three issues is final and is currently before the Courts of Appeals. Although the Commission appears to be reconsidering its ill-conceived maximum rate standards, it has not yet issued a new proposal.

The Staggers Act was the product of intense and sustained Congressional effort. Although the Act nearly died, it survived ultimately as a result of hard-fought compromises which are documented in its legislative history. The Commission, in its action on the issues discussed above, has ignored the balances painstakingly struck by Congress and should be required to account for its disregard of clear Congressional intent.

STATEMENT OF WILLIAM J. AUGELLO, ESQ., ON BEHALF OF SHIPPERS NATIONAL FREIGHT CLAIM COUNCIL, INC.

The Council appreciates the opportunity to bring to the Committee's attention several instances in which the Staggers Rail Act of 1980 has had adverse effects upon the shipping public and require remedial legislation. These matters pertain solely to carrier liability for freight loss, damage and delay claims, which has grown to a billion dollar problem annually for all modes of carriage.

Congress can no longer afford to ignore this problem which is dissipating our nation's natural resources and wasting precious energy and fuel to produce goods which never reach their intended destination—the consumer transit losses are avoidable and can be reduced, but not by reducing carrier liability standards and shifting the risk of loss from carriers to shippers, as suggested in Sec. 211(d) of the Staggers Act. The inducement to maintain and increase prevention programs can only be achieved by retaining and improving strict carrier liability standards.

The Interstate Commerce Commission has submitted its Report to Congress in Ex Parte 403 recommending the rejection of the suggestions contained in Sec. 211(d) of the Staggers Act which would have reduced carrier liability standards. The Council respectfully urges this Committee to accept the I.C.C.'s recommendations without changes, as the reasons given by the Commission for its position are sound and are based upon long years of expertise in this area.

In addition, the Commission urged adoption of three legislative amendments needed to remove inequities in the current position of carriers vis-a-vis claimants They are:

1. To repeal the venue changes enacted in Sec. 11707(d) of 49 U.S.C. in the Staggers Act;
2. To repeal the $10,000 minimum jurisdictional limitation on freight claim suits in the federal courts; and
3. To enact legislation providing for the recovery of attorney fees by successful claimants if the carrier failed to submit to arbitration.

Each of these recommendations is sound and have widespread support from the shipping public. The justification for these changes follow:

I. THE THREE CHANGES RECOMMENDED BY THE I.C.C.

1. Venue

Sec. 11707(d) of 49 U.S.C. was amended by the Staggers Rail Act of 1980, Sec. 211(c), to limit the places where a claimant may sue a railroad for freight loss or damage. The changes in Sec. 11707(d) deprive claimants of the right to sue either the origin carrier or delivering carrier in any jurisdiction having a connection with the through movement and in which the carrier is incorporated, licensed, "doing business," or "operated a railroad or route" (49 U.S.C. 11707(a)(1) and former section (d)).

These venue changes which were incorporated in the Staggers Act without prior notice to the shipping public, without public hearings, without consideration by the Judiciary Committees or the Bar, and without careful consideration by Congress, improperly deprive claimants of fundamental rights enjoyed by other citizens.

The venue changes enacted in Sec. 11707(d) were first disclosed on September 5, 1980, in the "compromise" version of the Staggers Act, and passed the House only four days later. The changes appearing in the final version of Sec. 11707(d) were made in Conference after an emergency meeting between the Council and another user group with the staff members of the House Interstate and Foreign Commerce Committee. Shipper interests did not agree to the final version of this provision. They did not see the final version until after its enactment.

At that meeting, the Council voiced objection to all of the proposed venue changes, citing one example where plaintiffs would be denied the right to sue a railroad at its principal domicile, such as the Southern Pacific Railroad in San Francisco. However, the final language adopted by the Conferees mysteriously translated this complaint into a new provision giving the claimant the right to sue at its principal place of business. (See 11707(d)(2)(A)(ii)).

Although claimants did not seek this change, there is no objection to it from this quarter. However, the Council has no objection to its repeal if the other amendments suggested herein are adopted.

This confusion over the issues and needs of the shipping public is a product of the haste with which this provision was drafted and rushed through the Congress. Without full disclosure and public debate, illogical, unreasonable and unlawful limitations have been placed upon claimants' rights.

The new law has the anomalous effect of permitting a general creditor or dissident stockholder to sue a western or southern railroad in New York, for instance but not a New York receiver of damaged goods which originated on that railroad. This right of election between suing the origin or delivering carrier has always been important to eastern receivers because of the substantial difference in the financial stability of western and southern carriers vis-a-vis eastern carriers. In essence, Congress has seriously impaired eastern receivers' ability to recover claims and suits quickly and with the least amount of expense.[1]

Consider also that certain claimants will also be deprived of the right to sue carriers in their own local courts when the final delivery is made by a switching carrier (as distinguished from a line-haul carrier). Sec. 11707(a)(1) precludes suits against such switching carriers, and the new venue restriction in subsection (2)(A)(ii) requires that the delivering carrier operate a railroad or route in the claimant's jurisdiction if it elects to sue at its principal place of business.[2]

It is ironic that, despite the current trend toward deregulation, Congress saw fit to increase the rules and regulations for litigants before the nation's courts. Even a cursory review of federal and state jurisdiction and venue provisions will show that the modern trend is to broaden, not restrict, the jurisdiction of the courts to dispose of actions relating to multi-state controversies. For example, the federal rules of civil procedure were amended in 1963 to provide for extraterritorial service of federal court process where the same is authorized by the law of the state in which the court sits. Professor Moore, noted commentator of federal court practice, has written that both state and federal courts are moving closer to the concept of nationwide jurisdiction over litigants.[3] That being so, restrictive venue provisions, such as enacted in Sec. 11707(d), are counterproductive and contrary to the trend of modern law.

Venue restrictions which significantly reduce the rights of a claimant to sue a defendant in his local state or federal court run afoul of rights reserved by the states for themselves and, therefore, is legislation proscribed by the United States Constitution.

In the Supreme Court case of *Pennoyer* v. *Neff*, 95 U.S. 714 (1877), it is written that "every state possesses exclusive jurisdiction and sovereignty over persons and property within its territory." Where jurisdiction exists but is nullified by restrictive venue provisions as under scrutiny here, the federal government makes an

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[1] Congress has also unintentionally and inadvertently increased the taxpayers' subsidy of Conrail, which will be forced to increase its staff of claims personnel and attorneys to process and defend the increase in claims and suits diverted to it from origin carriers as a result of the new restriction on venue.

[2] On traffic moving on the Southern Railway to St. Louis, MO, for example, the Southern's line ends in E. St. Louis, IL, and deliveries are made across the Mississippi River by a switching carrier. St. Louis, MO, consignees are now deprived of the right to institute an action in St. Louis even though the Southern Railway is doing business in that city and state.

[3] Moore, Moore's Manual of Fed. Practice and Procedure, Sec. 7.01.

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impermissible invasion into rights retained by the states for themselves and their citizens. The several states have the right to litigate the interests of their own citizens and this new statute will act in many cases to abrogate that right.

Present laws adequately protect defendants who feel aggrieved by the plaintiff's choice of forum for a lawsuit. The federal venue rules already have great flexibility in the provisions of 28 U.S.C. Sections 1404 and 1406. Those sections provide for the movement of cases within the federal court system from one district to another district not only where venue is improperly chosen, but also "for the convenience of parties and witnesses, in the interest of justice."

Within the state court system, a railroad carrier which finds itself brought into a suit in a forum which is abusive of its rights can easily avail itself of the common law doctrine of forum non conveniens to force dismissal of the action. Under the previously existing statutory scheme, claimants who took advantage of venue provisions which were unfair or burdensome toward rail carriers where always subject to dismissal or venue change under the previously cited sections. It is difficult to understand why the previous sanctions available to rail carriers are suddenly inadequate to protect them from abusive suits.[4]

Other technical changes in Sec. 11707(d) appear to be necessary for clarity. There is no justification for maintaining different venue conditions for rail v. motor carriers. The right to sue originating and intermediate carriers should be clearly specified. Each of these clarifications have been incorporated in the revision to Sec. 11707 annexed hereto as Appendix A.

These changes should also be made immune from I.C.C.-imposed exemptions under the provisions of Sec. 10505(e). In addition, Congress must codify its intent that Sec. 11707 not be repealed for any traffic exempted by the I.C.C. prior to the Staggers Act, namely, fresh fruits and vegetables traffic.

The reason for this request is that certain railroads are continuing to maintain provisions on exempt TOFC/COFC and fresh produce traffic which are in violation of Sec. 11707.[5]

Congress clearly prohibited variations from Sec. 11707 in Sec. 10505(e) of the Staggers Rail Act. Congress also expressed its intent that Sec. 11707 provisions be maintained on any traffic exempted from Sec. 11707 prior to the Staggers Act. However, some railroads have refused to honor this intent and continue to maintain short time limits and standards of liability lower than Carmack requires. The railroads apparently are relying on the fact that this intent was expressed in the Conference Report rather than in the statute and may be unenforceable.[6]

Sec. 10505 should be amended, therefore, as set forth in Appendix B.

2. The $10,000 Jurisdictional Threshold

One of the fundamental objectives of the Carmack Amendment as early as 1906 was to establish uniformity in carrier liability and claim practices for transportation in interstate commerce.[7] The object was to have all such matters controlled by uniform federal jurisdiction raher than varying application of 48 different state court systems.

Thus, no minimum jurisdictional amounts were originally imposed upon interstate claim litigation (28 U.S.C. 1337). However, effective October 20, 1978, the Committee on the Judiciary had legislation enacted, apparently without the knowledge of the transportation committees or the public, imposing a $10,000 minimum jurisdictional limitation on such actions in the federal courts. P.L. 95-496. This monumental change was induced by the fact that thousands of law suits on fresh

[4] A western carrier participating in a transcontinental movement to New York, for instance, would be required to send to a New York trial witnesses and evidence to prove its handling of the shipment, whether it was sued in New York, or the suit was brought against the eastern delivering carrier. This is inherent in our national transportation network, and our policy to make joint-line carriers jointly and severally liable for losses incurred anywhere on the joint-through movement. *Atlantic Coast Line R. Co.* v. *Riverside Mills*, 219 U.S. 186, 203–207 (1910). See *W.D. Lawson & Co.* v. *Penn Central Co.*, 456 F. 2d 419 (6th Cir. 1972).

[5] The Chessie System, for instance, continued in effect its $250 minimum claim provision and its 120 day claim filing limit and one year suit-filing limit on COFC/TOFC traffic as recently as September 21, 1981. The Santa Fe, on the other hand, maintained a six month limit and requires suits to be filed within one year of delivery (as distinguished from two years from disallowance of the claim as required by Sec. 111707) as recently as June 1, 1981.

[6] H.R. Report, No. 96-1430, p. 105: "For these reasons we also expect that except to the extent necessary to comply with subsections (e) and (g) of section 10505 of title 49 U.S.C. as amended by the Staggers Rail Act of 1980, an exemption order issued by the Commission prior to the effective date of the Staggers Rail Act of 1980 shall remain in full force and effect unless revoked pursuant to subsection (d) of section 10505 of title 49 U.S.C. as amended."

[7] Miller's Law of Freight Loss and Damage Claims, Richard R. Sigmon, 4th Edition 1974, pp. 9, 14; The Story of the Bill of Lading, National Freight Claim Council, ATA, p. 12.

produce claims were instituted in the federal courts in Boston by a small group of receivers and their claim agent.[8] The Committee on the Judiciary succeeded in having the law changed throughout the entire federal court system as a result of a problem which was localized in Boston and on rail produce claims alone.

As a result, claimants and all surface carriers have been deprived of uniform federal court decisions and policy by federal judges experienced in federal laws governing interstate commerce when the amount in issue is less than $10,000.

To illustrate the necessity for uniform federal law on interstate commerce, consider the decision rendered by the Supreme Court of Oregon, holding that a consignee is not bound by the time limits on a bill of lading because consignees are not a party to the contract of carriage.[9] This obviously is contrary to federal law. It is typical of the type of decisions that occasionally are rendered in state courts not familiar with interstate commerce law, practice or procedures.

The shipping public expressed strong objection to the $10,000 limitation in the Commission's study of rail liability.[10] The Commission responded by recommending repeal of this restriction. The I.C.C. states, at p. 40 of its Report to Congress:

"A new inconsistency exists now that Congress has recently removed the $10,000 threshold for original jurisdiction in federal question cases. (Pub. L. 96-486.) Today, federal question cases arising under the Carmack Amendment are treated differently from other federal question controversies. *Moore's Federal Practice* Section 0.167[4] asks, 'Why pick on Carmack Amendment cases when the balance of the Interstate Commerce Act, and all other federal laws, remain free of the over $10,000 limitation?'

"The Commision recommends removal of the new inconsistency so that Carmack Amendment controversies can be handled in the same manner as other federal question cases. Amending 28 USC Section 1337 and Section 1445(b) would be consistent with the Commission's recommendation that current venue restrictions for Carmack liability cases be repealed. We see no overriding justification for the disparate treatment simply because the defendant is a rail carrier. For the exclusive Federal jurisdiction that the carriers request, Congress would have to enact legislation."

The Council joins in this recommendation and urges that appropriate action be taken with the Judiciary Committee to remedy this inequitable restriction on claimants' remedies.

3. Attorney Fees and Arbitration

Congress enacted the first arbitration statute for transportation claims when it enacted Sec. 11711 of Title 49 in the Household Goods Act of 1980, P.L. 96-454, October 15, 1980. The need for a dispute settlement program for property claims is as urgently needed as was the need for household goods claims. The reason is that carriers have an advantage over claimants in that it is costly to litigate in the event a carrier refuses to voluntarily pay a lawful claim. In many cases, the expense of litigation exceeds the amount of the claim.

Accordingly, small property claims should be subjected to the same dispute settlement programs as Congress provided for household goods shippers. Although it may appear at first blush that property shippers are more sophisticated than household goods shippers, the Council's experiences during the past seven years indicates that there are more shippers who are unsophisticated in claims and carrier liability issues than those who are knowledgeable in these subjects.

The reason is that the administration of freight claims requires paralegal training. A freight claim is a legal demand for damages incurred as a result of the carrier's breach of the transportation contract and is governed by the law of bailments. Common carrier liability is governed by the common law (which is expressed in court decisions), by statutory law (such as the Carmack Amendment and the Bill of Lading Act), by international treaties (such as the Warsaw Convention and Carriage of Goods by Sea Act), by federal regulations (such as the I.C.C.'s rules in 49 C.F.R. 1005) by carrier tariff rules, and by the terms and conditions in bills of lading.

Relatively few shippers possess the training necessary to fully understand and apply these legal principles. Cariers, on the other hand, generally employ claims managers who are thoroughly trained and experienced in the law of carrier liability. The combination of superior training and the position of being in possession of

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[8] These suits were brought in Federal Court because of an evidentiary ruling in the State Court which held Federal inspection certificates inadmissible in the State Court. It was later overturned, but the practice continued. House Report 95-117, p. 50.

[9] *Lord Electric Co.* v. *Pacific Inter-Mountain Express Co.*, 1978 Fed. Carr. Cas. 82,781.

[10] The Santa Fe even suggested that the limitation be reduced to $3,000.

damaged goods and the funds necessary to pay for lost and damaged freight, places carriers in a superior bargaining position vis-a-vis claimants, particularly in light of the expense of litigation to compel payment.

This position frequently results in arbitrary declinations or unreasonable offers of compromise on lawful claims. Many carriers also refuse to divulge their record of handling shipments in transit. Others employ dilatory tactics and engage in "vexatious" conduct.[11]

The I.C.C. recommends equalizing the position of the parties by awarding attorney fees to successful plaintiffs who are forced to resort to litigation. It reasons that carriers would have an incentive to settle claims promptly and equitably, absent an equitable, efficient and inexpensive arbitration program (p. 55, Report to Congress).

The Council agrees. The provisions of Sec. 11711 enacted for household goods carriers should be considered for this purpose.

The Council strongly suggests that the provision for successful plaintiffs' attorney fees be adopted without provision for carrier attorney fees, except when the action was brought in bad faith. To allow attorney fees to carriers whenever they prevail would remove the incentives which the I.C.C. found to be necessary to equalize the position of the parties to claim disputes.

The Council urges, however, that the short time limit provided in the household goods program for submitting claims (Sec. 11711(d)(1)—120 days) not be adopted for rail or motor claims. This would have the undesirable effect of forcing all claims to be filed in less than nine months as the claimant would never know in advance whether it will need to arbitrate.

As the I.C.C. discovered and concluded in its study: "The Variety and complexity of shipping transactions argue against any shortening of the current time limits on filing claims and instituting litigation." (p. 47)

The I.C.C. noted that rail claims may be arbitrated by the American Arbitration Association under a program with the AAR.

As related to this Committee previously, the Transportation Arbitration Board has sucessfully arbitrated over 220 motor carrier claims in three years. It employs a novel two-arbitrator system using experienced carrier and claimant arbitrators on each panel. However, neither of these systems are completely satisfactory because they are voluntary.

The Committee is urged to adopt legislation which would extend the provisions of Sec. 11711 to claims against motor carriers, freight forwarders and railroads, except as noted herein with respect to the short time limit.

The Committee is also urged to explore the impostiion of a monetary limitation on the amount of claims which would be subject to this Section, such as $5,000 or $10,000 per shipment, as there is less need for a mandatory arbitration provision for larger claims.

II. THE COUNCIL'S ADDITIONAL RECOMMENDATIONS

A. Changes in Claim Rules and Practices Required in the Carmack Amendment (Sec. 11707)

1. Reasons for Disallowances

Congress enacted the first change in the Carmack Amendment (49 U.S.C. 11707) in 50 years at the request of this Council. I did so to reduce the unintentional outlawing of lawful claims caused by offers to pay part of a claim which did not state that the remainder of the claim was disallowed. Under the terms of former Sec. 11707, such compromise offers constituted a disallowance of part of the claim and thus started the two-year time limit for instituting suit. Sec. 11707(e)(1) now requires that offers of compromise specifically state that a part of the claim is disallowed and state the reason therefor.

A careful analysis of this amendment reveals that it addresses only half of the problem. It omits reference to disallowances of claims in whole. Presently, carriers can disallow the whole claim without furnishing justification. Sec. 11707(e) must be amended to govern all disallowances. Furthermore, the new requirement for stating a reason for the disallowance, while helpful to claimants, does ot fully address the problem of frivolous and improper disallowances.

For example, railroads frequently disallow claims on the ground that:

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[11] For the latest court decision involving dilatory tactics which resulted in the court awarding attorney and accountant fees under its equitable powers, see *Lewis W. Caspe, et al.* v. Aaacon Auto Transport, Inc., F. 2d (8th Cir. 1981) (1981 Fed. Carr. Cas. 82,951).

The pertinent portions of this recent decision have been reproduced in Appendix C.

1. One or more documents are missing (a practice declared by the I.C.C. to be improper);[12]
2. The amount of loss is not determined and stated within nine months (a practice declared by the I.C.C. to be improper);[13]
3. The claimant failed to furnish evidence that the carrier's negligence caused the loss (a practice which is in conflict with the common law burdens of proof);[14]
4. It has conducted that there is no carrier liability, either without conducting an investigation or without stating the facts upon which that conclusion is founded (as required in 49 C.F.R. 1005.4);
5. A connecting carrier caused the loss (Sec. 11707 makes originating and delivering carriers jointly and severally liable for all losses incurred en route, regardless of the ability of the carrier against whom the claim is filed to collect from the responsible carrier).

These and other improper disallowances would be quickly reduced by providing that the two-year time limit for instituting suit will not begin to run unless the carrier provided a "lawful" reason for its position.

The desired amendments to Sec. 11707(e) are set forth in Appendix A.

2. The "Receipt" of Disallowances and Claims

The conflict between the Judiciary Committee's version of when a disallowance shall start the running of the two-year time limit for instituting suit and the Transportation Committee's version as expressed in the Motor Carrier Act of 1980 was described in the Council's testimony before this Committee on July 9, 1981, and therefore, will not be repeated herein. There can be no doubt that the Committee responsible for drafting Sec. 11707(e) intended that the date of receipt govern this important notice.[15] We cannot account, however, for the official U.S. Code's adoption of the earlier enacted version in P.L. 96–258, which was made effective retroactively to October 17, 1978, in the "Codification Improvements Law" although the Motor Carrier Act was enacted later than P.L. 96–258.

The language enacted in the Motor Carrier Act of 1980 must be restored on equitable grounds, if on none other. Since the date of a carrier's receipt of a claim governs whether the claim has been timely filed,[16] it would be illogical not to apply the date of receipt by a claimant of a carrier's declination to start the two year suit-filing time limit. Whatever function is chosen (the mailing date or date of receipt), it should be the same for carriers as it is for claimants.

The Council respectfully submits that the date of receipt is the more logical and equitable to apply to the mailing of time-sensitive claim documents.[17] Remedial legislation should be enacted to rectify this conflict. The amendment needed to accomplish this result is contained in subparagraph (e) of Appendix A.

3. Codification of Ex Parte 263 Claim Regulations and Orders, and Prohibition of Exemptions Therefrom

In view of Congress' clear intent to retain and enforce the Commission's claim regulations as reflected in H. Rep. 96–1430, p. 105, and the susceptibility of these regulations to varying degrees of enforcement with changes in the makeup of the Commission and its changing attitudes and policies, the Council strongly urges that 49 C.F.R. 1005 be codified as a part of 49 U.S.C. 11707. (See Appendix A, new subsection (f).)

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[12] Question and Answer No. 11, Ex Parte 263 Order dated April 18, 1972.

[13] Question and Answer No. 1, Ex Parte 263 Order dated April 18, 1972.

[14] *Missouri Pacific Railroad Co.* v. *Elmore & Stahl,* 377 U.S. 134 (1964).

[15] "Subsection (b) amends section 11707(e) of title 49 to clarify when claims have been disallowed. Under the statute, the period for bringing a civil action against a carrier for a claim is computed from the time a person *receives* written notice from the carrier that the claim has been disallowed . . . Further, any communications *received* from a carrier's insurer will not constitute a disallowance, unless the insurer, in writing, informs the claimant of the disallowance and informs the claimant that the insurer is acting on behalf of the carrier." House Report 96–1069, p. 40. (Emphasis added)

[16] *Schaffer* v. *Pennsylvania R. Co.,* 127 N.Y.S. 2d 466 at 468, aff'd. 127 N.Y.S. 2d 468 (Sup. Ct., App. Term, 1st Department, 1952).

[17] Some cases hold that the mailing of a notice creates a presumption that it has been received, *Wichita Valley Ry.* v. *Davis,* 275 S.W. 169 (Civ. Ct. App. Tex. 1925); and that mailing in sufficient time to reach the addressee within the time limit in the ordinary course of the mails, shall be sufficient to prove compliance with the time limit. *Vencill* v. *Quincy, O. & K.C. R. Co.,* 112 S.W. 1030 (KC Ct. App. Mo. 1908). In *Burns* v. *Chicago, M, St. P. & P.R. Co.,* 100 F. Supp. 405, 409, a federal District Court held that "the date plaintiff's agent received copy of defendant's letter" governs the suit-filing time limit as a matter of law. Aff. 192 F. 2d 472 (8th Cir. 1951). In *Baldwin* v. *Fidelity Fire Ins. Co. of NY,* 260 F. 2d 951, at 957, a federal court held "It is not . . . the sending but the receipt of a letter that will constitute notice."

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A similar tactic was employed by Congress in 1958 when it codified the Commission's informal rulings on exempt commodities (Administrative Ruling 107) in 49 U.S.C. 302(b)(6). P.L. 85-625, August 12, 1958, 72 Stat. 573.

Codification of these claim rules will simplify the enforcement of the disallowance provisions suggested above and stabilize the administration of claims.

Furthermore, no justification exists for exempting any common carrier from these regulations. As previously demonstrated in the Council's July 9, 1981 testimony, when carriers are freed from claim regulations, they generally adopt unconscionable limitations of liability which are contrary to the public interest. The provisions of new subsection (g) contained in Appendix A should be adopted to prevent further abuses.

B. Limitations of Liability (Section 10730)

1. Full Value v. Limited Value Rates

By amending Sec. 10730 in three different Acts in 1980, (Motor, Rail and Household Goods), incongruous provisions have been created, and confusion over Congressional intent has resulted.

The common law requirement that full value rates be continued if a carrier elects to offer a lower rate in return for limited liability is clearly spelled out only in Sec. (b)(2) of Sec. 10730 governing motor carriers.[18] No similar provision appears in Sec. (a) governing household goods carriers and freight forwarders or in Sec. (C) governing railroads.

Did Congress intend to change this fundamental common law rule for rail, motor and household goods carriers? No such intent can be found in the legislative history of the 1980 legislation in which the laws were changed for these three modes. The I.C.C. agrees with the Council's position,[19] but the railroads do not accept this conclusion.[20] The I.C.C. has rejected the railroads' position in its Report to Congress at pp. 9–12. It concluded that *all* modes must offer full value rates if reduced liability rates are offered to shippers so that the shipper will have a reasonable choice of rates.[21]

However, Congress must clarify this intent. As the Commission correctly notes, the only support for this result is found in the legislative history of the Staggers Act.[22] As this Committee well knows, the courts are reluctant to interpret Congressional intent in the absence of ambiguous statutory language of a statute.[23]

The provisions of Sec. 10730(c) clearly provide an option for railroads to establish limited value rates without compelling the simultaneous maintenance of full value rates.

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[18] However, even this language is couched in permissive rather than mandatory terms; i.e., "The Commission may require. . ."

[19] See Ex Parte No. 390, Rail Rates Based On Limited Liability, December 22, 1980, wherein it held: "By this notice we are also reminding shippers and carriers that the new authority to publish limited-value rates without prior Commission approval does not in any way remove the carrier obligation, under the Interstate Commerce Act, to maintain full-value rates when shippers do not agree to released rates or where they desire full value as well as released rates. We do not view this as a problem for carriers. Existing full value rates may be complemented by released rates. So long as shippers have a choice between full and released value rates, there is no need to receive prior shipper approval for publication of the released rates (although it would still be subject to protest on other grounds such as unreasonableness.)"

[20] See AAR's opening statement in Ex Parte 403, Cargo Liability Study—Report to Congress, May 20, 1981, p. 9, footnote 10, wherein the railroads argue: "The railroad industry respectfully disagrees with the Interstate Commerce Commission's administrative ruling in Ex Parte No. 390, Rail Rates Based on Limited Liability. December 22, 1980. The language of this ruling appears to suggest that alternative, full liabililty rates are prerequisite for the establishment of Tier II limitation of liability rates under Section 10730, and perhaps for Tier I, limited liability contract rates under Section 10713. If so read, this administrative decision, arrived at without hearing would be contrary to the provisions of those sections which do not require alternate rates. For example, in sub-section (b) of Sec. 10730 Congress required the motor carriers to provide alternate rates but Congress did not require the rail carrier in sub-section (c) to provide alternate rates and no such mandate for alternative rates is contained in Sec. 10713. It must be noted that Sec. 10505, which deals solely with Interstate Commerce Commission exempt transportation, does prohibit the Commission from relieving railroads from Sec. 11707 liabililty on exempted traffic."

[21] It should be noted that the National Motor Freight Traffic Association also agrees that this provision should be mandatory and not merely permissive. See testimony of James C. Harkins, Executive Director, NMFTA and Paragraph 2 of Suggested Amendment—Limited Liability Rates, before the House Public Works Committee on the Motor Carrier Act, dated June 11, 1981.

[22] H.R. Report No. 96-1430, 96th Congress, 2d Session 102 and 105 (1980).

[23] *National Small Shipments* v. *Civil Aeronautics Bd.*, 618 F. 2d 819 (Dist. of Columbia 1980) at 828.

"(c) A rail carrier providing transportation or service subject to the jurisdiction of the Commission under subchapter I of chapter 105 of this title may establish rates for transportation of property under which the liability of the carrier for such property is limited to a value established by written declaration of the shipper or by a written agreement between the shipper and the carrier. . ."

"May" must be changed to "shall" in subsection (c), and a new subsection (d) must be added to require the same result with respect to all other modes. These amendments are set forth in Appendix D.

In addition, the Commission has noted an important defect in its power regarding this Committee's consideration.

The Commission properly observes at pp. 15–17 of its Report to Congress that in the absence of market dominance on any particular shipment, it no longer has the power to find a limited value or full value rate unreasonable.

"Thus, although rail carriers are required to offer full value rates in which their liability is not limited, where market dominance is not deemed to exist the ICC is virtually powerless to prohibit the carriers from setting their full value rates at an unreasonably high level, so as to force shippers to either accept lower priced released rates (which limit the carrier's liability), or take their traffic elsewhere." p. 16

"Arguably, a carrier who raises its full value rates to prohibitively high levels to force shippers to accept released rates may be engaging in an unreasonable practice in violation of 49 U.S.C. 10701(a). However, without jurisdiction over the rate level it would be difficult for the Commission to remedy this practice." p. 17

And, in its conclusions, at p. 63, the Commission states: "Without a clear Congressional statement to the contrary, the Commission will continue to require rail carriers to offer full value rates. However, the Commission wishes to point out to Congress that in the absence of market dominance, the only effect of this requirement may be the publication of excessively high full value rates in those cases where rail carriers choose to limit their liability. However, where market dominance exists, the Commission has jurisdiction to ensure the reasonableness of the total transportation package offered. Thus, where the Commission holds jurisdiction over rate reasonableness, it can ensure that full value alternatives are not offered at unrealistic rate levels. Hence, we do not recommend that the requirement that carriers offer full value rates be repealed."

Clearly, the Commission must have the power to find unreasonable a differential between limited and full value rates if shippers' common law right to a reasonable choice of rates is to be retained. The Commission appears to have such power for motor carrier rates pursuant to Sec. 10730(b)(1) and (2).

The Commission's concern that rail carriers would set their full value rates at unreasonably high levels to force shippers to accept lower liability rates is not mere conjecture. Several railroads have already taken such action.

For instance, the Atchison, Topeka and Santa Fe Ry. charges a 5 percent premium on TOFC/COFC traffic if the shipper elects to be subject to full Sec. 11707 liability. On exempt produce traffic, a penalty of 15 percent plus $350 was assessed by the Santa Fe for full liability.

These premiums for full liability protection previously available at the same or lower rates, are clearly unreasonable. They are designed to force shippers to accept lower liability at the same rates charged prior to deregulation.

It is respectfully submitted that this was not Congress' intent in amending Sec. 10730. At least the shipping public was led to believe that the traditional choice of rates would be preserved, but without the requirement for prior Commission approval. Traditionally, carriers offered a reduction from the full value rate in return for an agreement to limit the carrier's liability to a specified dollar amount (such as 50¢ a lb. or $50 maximum).

Accordingly, the Commission should be given jurisdiction over released rates to insure that there is a *reduction* in rates when liability is limited and that the differential between full value and limited value rates is reasonable, whether or not the railroad has market dominance on that traffic.

Sec. 10730 must be amended by adding a new subsection as follows:

"(d) Before a carrier may establish a rate for any service under this section, the Commission shall require such carrier to have in effect and keep in effect, during any period such rate is in effect, a rate for such service which does not limit the liability of the carrier. The Commission shall require that limited value rates shall be lower than the previously published full value rates, and that a reasonable relationship between full value and limited value rates be maintained whenever released rates are offered to the public."

Furthermore, no exemptions from Sec. 10730 should be permitted, as suggested in Sec. 10730(e) annexed as Appendix D. These amendments would put an end to a

source of conflict and expense to the federal government, carriers and the shipping public.

2. Deductibles

The Council strongly opposes the introduction of "deductibles" into bailment contracts, for the reasons explained in its testimony of July 8, 1981, before this Committee on the Motor Carrier Act of 1980. Briefly stated:

1. Deductibles have the adverse effect of providing carrier and other employees with a "license to steal";
2. Deductibles have application only in insurance contracts where the insured retains possession and control over the insured goods, and can protect them;
3. Deductibles are inappropriate in bailment contracts where the owner of the goods relinquishes possession of the goods to the carrier and is at the carrier's mercy to protect the goods while in transit;
4. Deductibles will tend to increase losses in transit and result in increased consumer costs; and
5. Deductibles violate the common law prohibition against exculpatory clauses which relieve a carrier of the consequences of its negligent acts.

The Council urges, therefore, that Sec. 10730(c) be amended to delete the last portion of that paragraph permitting deductibles in railroad agreements. No such contracts between railroads and shippers are known to be presently in effect after one full year of this novel provision. Those railroads attempting to introduce deductibles into rate agreements have been rebuffed by shippers, and the intitial transportation agreements containing such clauses have been withdrawn.[24]

In the event this Committee is unwilling to repeal the deductibles provision in Sec. 10730(e) as requested, Congress must at least clarify its intent to confine the right to introduce deductibles into railroad agreements only, and not for other modes. The Congressional intent to limit deductibles to this one mode is apparent from its amendment of all three paragraphs in Sec. 10730 during 1980,[25] but confining deductibles to subsection (c) governing railroads.

However, the Interstate Commerce Commission has reached a different conclusion with respect to a household goods carrier's application for a released rate including a novel deductible clause.[26]

This matter is being reviewed by a federal court at great expense to the shipping public and the governement.[27] If the Congress will not repeal deductibles for railroads as urged by this Council, Congress can readily reaffirm its intent to provide for deductibles in railroad rates by simply adding a new subsection (f) to Sec. 10780 as follows:

"(f) Deductibles may only be included in written agreements between shippers and railroads."

C. Miscellaneous Recommendations

1. Mandatory Cargo Insurance For Railroads

Although the I.C.C. requires the maintenance of cargo insurance by motor carriers and freight forwarders before certificated operations are permitted (49 C.F.R. 1043 and 1084), it lacks statutory authority to require railroads to hold similar cargo insurance for the protection of the public.

In view of the financial condition of railroads in recent years, Congress is urged to empower the I.C.C. with authority to prescribe mandatory minimum insurance limits. The Commission recommended this legislation as long ago as 1972 in conjunction with its decision in Ex Parte 263, 340 I.C.C. 515, at 721–2.

The Council urges enactment of similar legislation for railroads to protect rail shippers from future financial failures, particularly in light of the Congressional policy for increased competition, which appears to be resulting in increased financial pressures on carriers of all modes.

[24] See for example Item [illegible] in the Southern Pacific's TOFC/COFC tariff circular No. 1000 which contained a [illegible] deductible, but which was rescinded effective May 14, 1981. Similarly, The Family Lines rescinded its [illegible] minimum claim rule effective May 12, 1981.

[25] In the Motor Carrier Act of 1980, the Staggers Rail Act of 1980, and the Household Goods Transportation Act of 1980.

[26] Released Rates Decision No. FF-[illegible], Interstate International Inc. Used Household Goods, decided August [illegible], 1981.

[27] [illegible] National Freight Claim Council, Inc. et al. v. Interstate Commerce Commission and United States of America, No. [illegible] (U.S. Ct. of App. [illegible] Cir.). This action has been placed on the inactive calendar until March [illegible], 1982, to provide plaintiffs an opportunity to seek clarification by Congress and/or reconsideration by the Commission.

2. Creation of a Study Commission

The Council urged this Committee, in connection with the oversight hearings on the Motor Carrier Act of 1980, to appoint a STUDY COMMISSION to explore the:

1. Transfer of Sections 10730 and 11707 into the Bill of Lading Act, 49 U.S.C. 81-124; and
2. Rewrite the Uniform Straight Bill of Lading "in plain English."

The Council concluded that: "A workable and efficient national transportation system requires uniform liability rules and practices for *all* modes. The shipping public should not be subjected to entirely different liability regimes when dealing with motor carriers v. rail carriers v. air carriers, expecially in this day of intermodalism and active competiton among different modes. A proper legislative goal should be a uniform statutory structure for all types of carriers. We respectfully submit that this objective should be the subject of an indepth study by a qualified study group working under the auspices of this Committee."

We wish to reiterate the ugent need for these reforms and offer the Council's full resources to aid the Committee in achieving these worthy objectives.

It is respectfully urged that the recommended legislative amendments and actions submitted herein be acted upon at the earliest practical opportunity to prevent further abuses and actions adverse to the shipping public.

APPENDIX A

SNFCC'S REQUESTED AMENDMENTS TO 49 U.S.C. 11707(d) (THE CARMACK AMENDMENT)

Sec. 11707

(d)(1) A civil action under this section may be brought against [a] *an originating or* delivering carrier [other than a rail carrier] in a district court of the United States or in a State court *against the carrier alleged to have caused the loss or damage, in the judicial district in which such loss or damage is alleged to have occurred.* Trial, if the action is brought in a district court of the United States, is in a judicial district, and if in a State court, is in a State, through which the defendant's carrier operates a railroad or route.

(2) A civil action under this section may be brought in a United States district court or in a State court *without limitation of the amount in controversy.*

(3) In this section, "judicial district" means (i) in the case of a United States district court, a judicial district of the United States, and (ii) in the case of a State court, the applicable geographic area over which such court exercises jurisdiction.

(e) A carrier may not provide by rule, contract, or otherwise, a period of less than 9 months for filing a claim against it under this section and a period of less than 2 years for bringing a civil action against it under this section. The period for bringing a civil action is computed from the date [the carrier gives a person] *a person receives* written notice *from* [that] the carrier *that it* has disallowed any part of the claim specified in the notice. For the purpose of this subsection—

(1) disallowances in whole or in part by carriers or their agents shall not start the running of the time limit to institute a suit unless the carrier, in writing provides a lawful reason for said disallowance.

(2) an offer of compromise shall not constitute a disallowance of any part of the claim unless the carrier, in writing, informs the claimant that such part of the claim is disallowed and provides reasons for such disallowance; and

(3) communications recieved from a carrier's insurer shall not consitute a disallowance of any part of the claim unless the insurer, in writing, informs the claimant that such part of the claim is disallowed, provides *lawful* reasons for such disallowance, and informs the claimant that the insurer is acting on behalf of the carrier.

(f) Carriers shall dispose of claims in accordance with regulations and orders promulgated by the Interstate Commerce Commission in Ex Parte 263, 340 I.C.C. 515 (49 C.F.R. 1005).

(g) No common carrier shall be exempted from the provisions of this Section unless specifically authorized by statute.

APPENDIX B

SNFCC'S REQUESTED AMENDMENTS TO 49 U.S.C. 10505 (EXEMPTION POWERS)

Sec. 10505

"(e) No exemption order issued pursuant to this section shall operate to relieve any rail carrier from an obligation to provide contractual terms for liability and

claims which are consistent with the provisions of section 11707 of this title. Nothing in this subsection or section 11707 of this title shall prevent rail carriers from offering alternative terms [nor give the Commission the authority to require any specific level of rates or services based upon the provisions of section 11707 of this title.] *and the Commission shall have the authority to determine the reasonableness of the alternative terms.*

Any exemption order issued by the Commission prior to the enactment of this section shall be modified by the Commission to comply with this subsection, if necessary.

Appendix C

[Cited 1981 Federal Carriers Cases *Caspe v. Aaacon Auto Transport, Inc.*]

* * * but to leave the inside of the car free for the driver's luggage and any passengers. Thus, the purpose of putting luggage in the trunk only does not appear to be to limit liability with regard to such luggage. In addition, even if the briefcase and records had been placed in the trunk as requested, they still would have been stolen along with everything else. Thus, this argument has little merit.

We conclude under the facts of this case, that the harm for which the district court allowed a recovery was not so unforeseeable as to make damages for the loss unrecoverable.

Finally, there is the question of attorneys' fees. It must be recalled that plaintiffs' attorneys dealt unsuccessfully with Aaacon several months before filing suit, and then the case itself took approximately three and one-half years to reach trial. We have reviewed the record submitted to us on appeal, and agree with the district court's conclusion that defendant's conduct was "most vexatious." [7] Under *Alyeska Pipeline Co, v. Wilderness Society,* 421 U.S. 240, 254–59 (1975) the court had the inherent power to award attorneys fees in such a case. *Miller v. Aaacon Auto Transport, Inc.,* 447 F. Supp. 1201, 1207 (S. D. Fla. 1978). Because appellant has failed to provide us with the actual court order awarding the fees, and we have seen at least four different numberical amounts [8] in documents provided to this court, we consider that appellant is merely questioning whether attorneys fees can be awarded, not the amount so awarded. However, by all indications, the district court did not abuse its discretion in that regard.[9]

The judgment and order of the district court is affirmed in all respects.

Appendix D

SNFCC'S REQUESTED AMENDMENTS TO 49 U.S.C. 10730 (THE CARMACK AMENDMENT)

Sec. 10730. Rates and liability based on value

[7] As mentioned earlier, appellant failed to comply with a court order to produce certain documents and to answer interrogatories. Instead, it filed a motion for partial summary judgment, requesting that the court rule on it with all due speed. A second order was necessary. Over one year after discovery was closed, Aaacon scheduled two depositions on the same day in different regions of the country. It refused to give local counsel any authority to stipulate to anything at the pre-trial conference, and did not provide a witness list or exhibit list, and indicated no witnesses or exhibits would be offered at trial. As a result, a magistrate entered an order prohibiting Aaacon from having any witnesses at the trial, although they were allowed to introduce exhibits. In addition, there were numerous motions and requests for continuances which prolonged the proceedings. As stated in plaintiffs' Combined Application for Continuance of Oral Depositions and Protective Order:

The amount in controversy is less than ten thousand dollars; and were these average Plaintiffs this action would have died long ago through the exhaustion of Plaintiff's resources and will.

[8] It was stated in appellant's brief at 28 that the court concluded $4,133 of plaintiffs' legal fees was attributable to vexatious conduct, and at page 30 that the trial court granted $3,970. Appellee's brief at 19 indicates that $4,100 was the amount found by the lower court to be attributable to vexatious conduct. Finally, there is reference in a later order awarding plaintiffs further attorneys' fees with regard to a post-trial motion made by defendants (Aaacon does not appeal that award here) and reprimanding Aaacon's local counsel in which the court itself refers to the earlier award as $3,980.

[9] The amount requested for attorneys fees was $11,175.10, which is more than the total amount involved in this case. We have no doubt that the lengthy proceedings involved over four years could indeed generate a bill of this size. Aaacon hardly has to worry about its legal bills, since it is owned by Ralph Zola, the head of Zola and Zola, a law firm who presented the appeal in this court and who was primary counsel in the lower court. If unfair tactics have been or are used by Aaacon, then persons like Caspe are necessary to establish principles needed to insure that justice ultimately prevails.

(a) The Interstate Commerce Commission may require or authorize a carrier [(including a motor common carrier of household goods but excluding any other motor common carrier of property and excluding any rail carrier)] *of household goods and freight forwarders* providing transportation or sevice subject to its jurisdiction under subchapter [I,] II, or IV of chapter 105 of this title, to establish rates for transportation of property under which the liability of the carrier for that property is limited to a value established by written declaration of the shipper, or by a written agreement, when that value would be reasonable under the circumstances surrounding the transportation. A rate may be made applicable under this section to livestock only if the livestock is valuable chiefly for breeding, racing, show purposes, or other special uses. A tariff filed with the Commission under subchapter IV of this chapter shall refer specifically to the action of the Commission under this section.

(b) [(1) Subject to the provisions of paragraph (2) of this subsection, a] *A* motor common carrier providing transportation or service subject to the jurisdiction of the Commission under subchapter II of chapter 105 of this title may, subject to the provisions of this chapter, (including the general tariff requirements of section 10762 of this title), establish rates for the transportation of property (other than household goods) under which the liability of the carrier for such property is limited to a value established by written declaration of the shipper or by written agreement between the carrier and shipper if that value would be reasonable under the circumstances surrounding the transportation.

[(2) Before a carrier may establish a rate for any service under paragraph (1) of this subsection, the Commission may require such carrier to have in effect and keep in effect, during any period such rate is in effect under paragraph, a rate for such service which does not limit the liability of the carrier.]

(c) A rail carrier providing transportation or service subject to the jurisdiction of the Commission under subchapter I of chapter 105 of this title may establish rates for transportation of property under which the liability of the carrier for such property is limited to a value established by written declaration of the shipper and the carrier. [, and may provide in such written declaration or agreement for specified amounts to be deducted from any claim against the carrier for loss or damage to the property or for delay in the transportation of such property.]

(d) Before a carrier may establish a rate for any service under this section, the Commission shall require such carrier to have in effect and keep in effect, during any period such rate is in effect, a rate for such service which does not limit the liability of the carrier. The Commission shall require that limited value rates shall be lower than the previously published full value rates, and that a reasonable relationship between full value and limited value rates be maintained whenever released rates are offered to the public.

(e) No common carrier shall be exempted from the provisions of this section unless specifically authorized by Statute.

Statement of Carolina Power & Light Co., Duke Power Co., South Carolina Electric & Gas Co., and Virginia Electric and Power Co.

Carolina Power & Light Company, Duke Power Company, South Carolina Electric & Gas Company, Virginia Electric and Power Company appreciate the opportunity to present their views in these Legislative Oversight Hearings on the administration of the Staggers Rail Act of 1980, Public Law 96–448.

IDENTIFICATION OF THESE PARTIES

These companies are engaged in the generation, sale and distribution of electrical energy to customers in the states of North and South Carolina, Virginia and West Virginia. They rely upon the railroads for the transportation of millions of tons of bituminous coal to their coal-fired electric generating stations. Their annual bill for the rail transportation of such coal is well in excess of $200,000,000.

Accordingly, they are substantially and directly affected by the Staggers Rail Act of 1980 as well as the manner of its administration.

APPROACH TAKEN IN THESE COMMENTS

These four utility companies are well aware of the fact that the Surface Transportation Subcommittee in its Oversight Hearings has already developed a substantial record both in scope and in depth. Accordingly, these companies will not repeat in detail the points made by other witnesses with whom they strongly agree. Rather, they will present the key matters on which they wish to place their emphasis.

MANNER OF HANDLING THE VARIOUS FORMAL PROCEEDINGS UNDER THE STAGGERS RAIL ACT

Because of their obvious interest in and concern with the implementation of the Staggers Rail Act these companies have been parties to most of the key proceedings activated by the Commission. Indeed they are also parties to several of the court proceedings which have been brought attacking the actions taken by the Commission.

Almost without exception, particularly in the earlier proceedings, the Commission saw fit to depart from the normal practice of (1) establishing a service list, (2) providing due dates for the filing of Opening and Reply Statements and (3) thereby according parties the opportunity to analyze and comment upon filings of other parties.

Indeed, it was often extremely difficult either to ascertain who were the other parties in these proceedings or to obtain copies of their filings.

By this short-cut procedure the Commission deprived itself of adequate records upon which to reach the ultimate findings and conclusions. The Congress should make clear to the Commission that this type of omission should not be repeated to the extent that any future proceedings are activated.

RAILROAD MARKET DOMINANCE

These companies recognize that the Congress was prepared to allow the forces of the market place to govern where there was genuine, effective competition present to protect the interests of the shipping public. At the same time, the Congress was careful to preserve the regulatory power of the Interstate Commerce Commission where such effective competition was not present.

The 4R Act definition of market dominance is still in effect:—". . . an absence of effective competition from other carriers or modes of transportation, for the traffic or movement to which a rate applies. . ."

It is the emphatic view of these companies, who are confronted with railroad market dominance, that the Congress intended that captive shippers be protected from railroad abuse of market power.

Respectfully, these companies are of the view that the Commission is failing to administer the law so as to ensure such protection to shippers confronted with rail monopoly or oligopoly.

The Commission arbitrarily and capriciously terminated several practical, realistic rebuttable presumptions as to market dominance which has been carefully evolved in proceedings upon very complete records and which were upheld upon court review by the U.S. Court of Appeals for the District of Columbia Circuit.

Rather, the Commission has both terminated such rebuttable presumptions and has also instituted in their stead vague evidentiary guidelines. Beyond that, in disregard of the transportation standard embodied in the above-quoted statutory language the Commission has brought to the fore the concepts of product and geographic competition.

The latter, now under bitter attack on court appeal by many parties, including these companies, will, if tolerated, go far to undermine if not destroy the railroad market dominance provisions intended to protect the shipping public.

The Congress should make clear to the Interstate Commerce Commission its statutory intent and leave the Commission in no doubt that the Agency has veered off-course.

RAILROAD COST INDEXING

These companies have been profoundly disturbed by the Commission's approach to the implementation of Section 203 of the Staggers Rail Act, 49 U.S.C. § 10707a. The Commission appears to be relying all but totally upon data being unilaterally furnished by the Association of American Railroads (AAR). At the threshold here a fundamental error is being made in that the railroads and the Commission are utilizing "prices" rather than "costs" in establishing a cost index. This is erroneous on its face and, of course, is extremely injurious to the shipping public.

Beyond that, the shipping public is given no opportunity to analyze the underlying data and the methodology utilized by the railroads and submitted unilaterally to the Commission. This is a species of "quasi star chamber" which is incompatible with the long established principles of due process and fair hearing.

DETERMINATION OF RAILROAD COST OF CAPITAL

The Commission in this phase of the implementation of the Staggers Rail Act has seen fit to confer windfalls upon the railroads. For example, the Commission has seen fit to reverse itself in mid-stream and is injecting into the calculation of railroad cost of capital "current" cost of debt in utter disregard of the historical cost of debt actually incurred by the railroads.

These companies here point out that we are dealing with railroads being regulated under the federal transportation laws enacted by the Congress with respect to railroads. We find nothing in these laws applicable to the railroads to warrant such an approach at the expense of those who must pay and bear railroad freight rates.

DETERMINATION OF RAILROAD REVENUE ADEQUACY

The Commission has gone so far a field in this area that practically every railroad in the country, with two or three minor exceptions, is now designated as revenue inadequate.

This is occurring at a time when the nation's financial press is heralding the splendid records being achieved by carriers such as Southern Railway System, Chessie System, Union Pacific, Burlington Northern, The Family Lines and many others.

A CRUCIAL GOAL OF THE STAGGERS RAIL ACT

The Congress in Section 3 of the Staggers Rail Act specifically declared as one of the goals of the law: ". . . to provide a regulatory process that balances the needs of carriers, shippers, and the public . . ."

Carolina Power & Light Company, Duke Power Company, South Carolina Electric & Gas Company, Virginia Electric and Power Company firmly believe that the Congress meant what it said when it enacted the above-quoted language. At the same time these companies express their deep concern that the Commission may be giving lip service to the above-stated goal but with respect to the matters above discussed (and others) is approaching the implementation of the Staggers Rail Act disproportionately in terms of the interests of the railroads. This is, in the view of these companies, illustrated, for example, in the Commission's treatment of railroad market dominance and in the Commission's treatment of the railroad cost indices under Section 203 of the Staggers Rail Act of 1980.

CONCLUSION

The foregoing is not intended to be an exhaustive narration of the concerns of these companies. Indeed, there are others. The objective here is to stress some of the more egregious aberrations on the part of the Commission in purporting to implement what Congress enacted in the Staggers Rail Act of 1980.

Carolina Power & Light Company, Duke Power Company, South Carolina Electric & Gas Company, Virginia Electric and Power Company appreciate the opportunity to submit these views to the Subcommittee. They ask that they be made part of the official record of these hearings.

STATEMENT OF WALTER H. CRAMER

Mr. Chairman and Members of the Subcommittee, I appreciate this opportunity to present you some smaller Class I railroads' review of their first year of experience under the Staggers Rail Act. It has been a deeply disturbing experience, as I will show you through this statement.

At the outset, let me tell you about the companies I represent and where they fit into the Committee's area of responsibility. I serve as a Vice President for a group of railroads owned and controlled by the Grand Trunk Corporation.

RAILROAD AND MAJOR STATE SERVED

Central Vermont Railway, Inc., Vermont; Detroit, Toledo and Ironton Railroad Company, Ohio; Duluth, Winnipeg and Pacific Railway Company, Minnesota; and Grand Trunk Western Railway Company, Michigan.

Grand Trunk and DT&I are Class I railroads, and CV and DWP are Class II carriers under ICC reporting requirements. All four are progressive regional railroads, setting service standards for the territories they serve.

Unlike many railroads in their service areas, these companies have, with but few exceptions, consistently produced transportation service at a profit. They pay taxes,

in addition to providing outlets to the national economy for the basic industries they serve. While the Northeastern Regional Economy has been painted in bleakest tones to Congress, CV, DT&I and GTW have been able to exist in that same regional economy by providing consistent service to their shippers—a service second to none. With a track structure maintained to the highest standard, these service oriented railroads are accustomed to making the competition by which railroads are measured. Since that competitive ethic is what the Staggers Rail Act sought to establish and encourage, we should have welcomed the Act. We did welcome the passage of the Act, and we commend Congress for its wisdom in this measure, on an overall basis, just as we appreciate these oversight hearings at the end of its first year.

Nevertheless, I must tell you that the Act must be significantly tightened, and its administration must be carefully monitored, or many smaller railroads (like my own) may not exist by the time of your second or third oversight hearings. I will show you how the rate setting and route closing freedoms set out broadly in the Act are being misused in massive fashion to create predatory practices which the Congress could never have conceived—indeed, practices which I believe Congress expressly attempted to preclude. Loopholes exist in this new law which are being abused to create a climate where more Class I railroads can be forced into the same straits where Conrail has languished for the past ten years.

Like so many laws, mechanical or unsympathetic administration of its literal or loose language can ultimately subvert the purpose for which Congress enacted it. We see dangerous symptoms of this malaise in the first year of the Staggers Act's existence.

President Dempsey of the AAR has previously testified (at page 25 of his testimony here):

"Joint Rates: The purpose of section 217, Compensatory Joint Rate Relief, was to provide a method whereby a carrier could, with a minimum of regulatory interference, get out of an uneconomic joint rate or route. Conrail viewed this as one of its most acute problems. Actions taken by Conrail and other railroads under this section have in some instances given rise to complaints by connecting carriers. In several instances litigation is pending. Because the views of the AAR members differ on the manner in which this section is being used, I will leave any expression of views to the members."

Mr. Dempsey wisely reserved judgment on this issue, I believe, for nothing has so strongly divided this industry as what we regard the ruthless strategies devised by Conrail to run roughshod through the loopholes of the Staggers Act. While these are strong words, I believe that they are clearly documented by the public record. And we are deeply disturbed that it is Conrail, which has received billions of dollars in public funds, which is taking this anti-competitive action. The cruelest cut, however, is that we perceive Conrail to be dissipating its own profitability by these predatory route cancellations so that if and when it emerges as a private sector company it will have eliminated its principal competitors. We suggest to the Committee that these steps appear to be a serious misuse of both the U.S. Treasury and certain loosely drawn provisions of the Staggers Act. I shall provide specific details here of how these things are now taking place, being portrayed as "the will of Congress".

We perceive the most glaring perversion of Section 217 to be shown by one presently pending case. ICC 38676 involves Conrail's closing of over 100,000 through routes in one fell swoop. By removing from the basic routing guides almost all routes except Conrail's longest long haul routes on interterritorial freight traffic,[1] Conrail effectively cancelled almost all through routes we previously possessed with it to handle traffic (between Chicago and Buffalo, for example) destined to and from Conrail served industries in the East. In these examples, a shipper routed the car GTW east of Chicago (to Buffalo thence Conrail to destination) in order to get the expedited service which we produce. The shipper always had the right to route via Conrail all the way east of Chicago. But because Conrail was unable or unwilling to provide satisfactory service, the shippers often favored us with the routing to intermediate points such as Buffalo and Detroit. These routes have existed since the ICC prescribed them (in its Docket 28300) many years ago and provided the basis for extensive competition among railroads for "overhead" traffic (traffic moving between points which the handling railroad does not serve). Seattle to Boston traffic, for example, is overhead traffic to GTW, since we can handle it only between Chicago and Buffalo—if the routes are open and if the shipper prefers our service. By cancelling all of these routing guide routes, Conrail took away the shipper's right to designate our service on such (Transcontinental) traffic.

[1] Transcontinental Territory to Eastern Territory, for example.

The only action which Section 10705a(c) permits a rail carrier to take without consent from its connections is "[to] cancel the application of *a joint rate to a through route.*"[2] Congress' express purpose in providing carriers with this limited new authority "was to ensure that no rail carrier would be compelled to carry goods unless its share of the revenues from the joint rates . . . is at least 110 percent of the carrier's variable cost of providing the particular services involved." Joint Explanatory Statement of the Committee on Conference on S. 1946, S. Rep. No. 96-1430, 96th Cong., 2d Sess. 108 (1980).

Rate cancellations were to be prevented where there was a demonstration either that the cancelling carrier's share of the revenues under the joint rate is equal to or greater than (A) 110 percent of its variable cost of providing service of such route, or (B) such lesser percentage of the variable cost than the cancelling carrier earns over a competing through route to which application of the joint rate has not been cancelled, or over a competing single-line route. 49 U.S.C. 10705a(c)(2).[3] Thus, the plain language of Section 10705a(c) amply demonstrates that it was intended only to permit the unilateral cancellation of specific joint rates on particular through routes and not, as Conrail has done, the wholesale cancellation of the application of almost all interline through routes to such joint rates.

This conclusion is confirmed by the Act's own legislative history. Thus, the House Committee on Interstate and Foreign Commerce observed that Section 10705a(c) authorizes a carrier "to cancel the application of a *joint rate* to a *particular through route* subject to that rate." *H.R. Rep. No. 96-1035*, 96th Cong., 2d Sess. 64 (1980). Moreover, the *Conference Report* emphasized that this subsection "establishes procedures by which rail carriers which do not earn adequate revenues under existing *joint rates* and divisions can . . . cancel their application to *particular* routes without the concurrence of other carriers." *Report of the Commission on Conference on S. 1946*, Rep. No. 96-1430, 96th Cong., 2d Sess. 108 (1980). (Emphasis supplied.) The ICC has ruled in *Ex Parte 389* that a railroad could only cancel the application of a *specific* joint rate on *specific* commodities over a *specific* route if it chose to use the summary procedures of Section 10705a(c). The Commission expressly found that in assessing a proposed cancellation under Section 10705a(c) "[t]he focus would properly be on the general profitability of a specific commodity moving over a particular route." 46 Fed. Reg. at 19240. The Commission similarly emphasized that "joint rate cancellations are selective in nature and will not apply to the vast majority of commodities moving by rail." *Id.* at 19241. The Conrail cancellations at issue in Docket 38676 are thus *far* outside the intended scope of Section 10705a. Conrail's tariffs do not cancel, as contemplated by the Act, *specific* joint rates on *specific* commodities over *specific* routes. Instead, Conrail has closed virtually all *interline routes* in its service territory where it also participates in routings it prefers—*i.e.* Conrail local routes and interline routes which afford Conrail its maximum haul.

We see this as misuse of the Staggers Act. To thousands of cities and industries served by Conrail, shippers are thus remitted solely to the service of Conrail. Before these route cancellations, shippers who could not get adequate service minimized Conrail's participation in through traffic by routing via alternative routes to Eastern junctions with Conrail. Conrail's action has systematically eliminated that shippper option, leaving industry with only the routes Conrail chooses to provide.

These questions were raised at the formation of Conrail, and both USRA and the ICC responded to demands by local government and many shippers by insisting that Conrail maintain and keep open these same through routes. DT&I and GTW have written contracts with Conrail which obligate it to maintain and keep open these routes which it has closed. We have addressed these facts and these concerns specifically to the ICC in connection with Conrail's present massive route closing program, yet it permitted these closings to become effective, by a vote of the entire Commission in ICC 38676.

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[2] That provision states in full: "Notwithstanding any other provision of this title, any prior agreement in effect on the effective date of the Staggers Rail Act of 1980, or any requirement of the Commission, a rail carrier *may cancel the application of a joint rate to a through route* in which it participates, without the concurrence of any other rail carrier that is a party to such *joint rate*, unless another rail carrier that participates in such through route or a shipper that has no competitive alternative to such route makes the demonstration described in paragraph (2) of this subsection." (Emphasis supplied.)

[3] Section 10705a(c)(4) provides that where the showing under Section 10705a(c)(2) has been made, "the existing joint rate should remain in effect during the pendency of the Commission's consideration" of the lawfulness of the rate. Although the Commission found in Docket 38676 that the protesting railroads had demonstrated here that a substantial number of Conrail's cancellations were unlawful under Section 10705a(c)(2) the Commission failed to suspend the cancellations in its July 24, 1981 order instituting an investigation into the lawfulness of those cancellations.

In our protests we showed how many of the routes Conrail was closing to us returned to Conrail far in excess of the 110 percent of its variable costs specified by § 217. Indeed, the Commission expressly found in its 38676 order that: "Various protestants have demonstrated that a substantial number of shipments of particular articles from specific origins to specified destinations via affected gateways move at single-factor-joint rates that provide Conrail with revenue equalling or exceeding 110 percent of its variable cost of providing service over the route or routes."

Yet, despite this finding, the Commission failed to suspend even one of the Conrail route closings.

Indeed, we petitioned the Commission to reject entirely Conrail's proposed route closing tariffs, since they appeared absolutely inconsistent with both the law and its legislative history, which states plainly that its procedures are to be used for cancelling the application of *a* particular joint rate to *a* through route, rather than wholesale cancellations of hundreds of thousands of routes at one fell swoop. The cancellations were neither rejected, nor suspended, and, as a result, we are out of business entirely on routes which provided over $50 million in business each year to Eastern railroads other than Conrail.

Look carefully at this result. Conrail was shown to earn more than 110 percent of its variable costs on this through route business with us. It was profitable business to Conrail, which is a very high cost Class I railroad. Yet Conrail arbitrarily cancelled our participation in this, its own profitable business. My people investigated to see whether the single line routes it retained were really more profitable to Conrail than the portion of the through revenue it formerly obtained. We were able to obtain discovery of some such data by virtue of ICC orders compelling Conrail to make discovery, and we discovered that more often than not Conrail was earning lower profits (measured as ratios of Conrail's revenues to its long term variable costs) on its own single line routes than it obtained from its share of the through route earnings. Conrail's own records showed that on 1,391 (out of 1,501) of our carloads measured by Conrail's data, it earned lower ratios on its own single line route than it earned in the former through earnings with us.

I respectfully submit that neither these facts, nor the business strategy that I deduce Conrail is implementing (derived from these facts), is consistent with the stated goals of the Staggers Rail Act. For these reasons, I suggest that the law is being seriously misused, and that it needs careful tightening, either through Congressional revision or far more careful implementation by the Interstate Commerce Commission. When monopoly business strategies are imposed in the name of competition, something is seriously wrong, I respectfully suggest to the Committee.

I will be happy to respond to any questions that the Committee deems useful.

Statement of John A. Creedy, President, Water Transport Association

My name is John A. Creedy and I am president of the Water Transport Association of New York, a national trade association of "for hire" and ICC-certificated domestic water carriers operating on the inland rivers, the Great Lakes and in the coastwise and intercoastal trades.

Our organization took an active part in the hearings which eventually led to the passage of the Staggers Rail Act of 1980. We greatly appreciate this opportunity to appear at oversight hearings a little more than a year after the measure became law.

As everyone recognized at the time, the act is exceedingly complex. One can only admire the energy with which the ICC has set about implementing its many provisions. There have been over 35 proposed rule-making proceedings, many of which are still pending, about 40 final rules and 17 major policy statements interpreting the Act. Transportation lawyers have never been more actively engaged.

As is only to be expected, there is more than a little disagreement. The ICC finds itself defending nearly 20 court actions brought by railroads, shippers and the Water Transport Association.

In a sense, it is too early, for the water carriers anyway, to reach conclusions as to the immediate need for remedial legislation. We can, however, report on apparent trends in interpretations for your information, and remind this Committee of unfinished business in the task of improving the climate for healthy competition and intermodal coordination between rail and water carriers.

It is useful to review the rail transportation policy adopted by the Congress. A major objective of the new law of course was to provide substantial flexibility in rail pricing, relaxation of maximum rate regulation, new authority for contracting and exemption, and the expediting of mergers, among other objectives.

A primary objective of the policy is to ensure effective competition and intermodal coordination, and particularly "to prohibit predatory pricing practices, to avoid undue concentrations of market power and to prohibit unlawful discrimination."

Shippers brought forcefully to the attention of the Committee the plight of the so-called "captive"—the shipper with no effective transport alternative to a single railroad. The major shipper groups supported provisions that would safeguard existing and potential rail-water competition and coordination against abuse of monopoly power.

The water carriers testified that if competition is to be a main reliance in arriving at reasonable rates in the future, safeguards against undermining competition are essential. The major shipper groups endorsed the view that ground rules under which competition is conducted are highly desirable.

The question of stimulating intermodal competition and coordination has become more urgent in the light of the major mergers that are now proceeding under the new Staggers Act rules. Railroad leaders have predicted that the rail network may soon settle down to no more than six or seven major systems which will, of course, have unprecedented market power and unprecedented opportunities for abuse.

Size by itself, of course, need not be a problem, but well-worn and often-used tactics of rate manipulation by very powerful railroads can easily stifle competition.

In testimony before this Committee, we stressed the need to pattern control of abuse of monopoly power in transportation after the principles of the antitrust laws, which, after all, express the competition policy of the country for industry generally. We suggested clear prohibitions of abuses plus a treble damage deterrent—a customary feature of antitrust enforcement. Fear of money damages acts as a self-regulator of monopoly action. Self-regulation is much to be preferred and is far more effective than detailed government intervention.

The evil that needs controlling anywhere it appears in the economy is the abuse of economic power. Traffic won by the exercise of economic power or leverage serves only the private interest, whereas traffic won on the basis of superior efficiency serves the public interest.

Interestingly enough, in the UP-MP-WP merger proceeding before the Commission, Ben Biaggini, Chairman and Chief Executive Officer of the Southern Pacific, a large railroad, testified as to his concern that the merged railroad intended "to engage in destructive price competition."

The two anti-competitive tactics which historically have concerned water carriers and their shippers involve practices which have their counterparts in the unregulated economy and remedies in the antitrust arsenal designed to promote competition.

The first, as this Committee will recall, is the practice of "sharpshooting"—selective discriminatory price reductions which undercut the barge competition. No relatively small manufacturer confined to one locality or limited to a few product lines could withstand "sharpshooting" price reductions on the part of a national producer with superior economic power. No more could a barge line.

The remedy in transportation has been the same as in industry generally. Where there is a "sharpshooting" type of discrimination, there is a "meeting competition" test similar to that under the Robinson Patman Act. Abuses most often occur in rail-water competition in situations where a railroad charges less for a long haul along a route than for a short haul on the same route. The long and short haul provisions controlling such abuses was specifically preserved in the Staggers Act.

The other abuse—the "price squeeze" or "bottleneck monopoly" type of abuse, occurs where a railroad manipulates the connecting rail rate with a water carrier so as to frustrate a coordinated rail-water route in favor of an all-rail alternative.

Where a railroad seeks a barge connection of course, it can be sure of the "best efficiencies" by barge because it has 20 to 30 barge lines from which to choose. When a water carrier seeks a rail connection, it may be at the mercy of only one railroad. Arbitrarily setting a rate too high or refusing "best efficiencies" such as a unit train can readily undermine healthy competition and preclude a shipper from receiving a more efficient service at a lower overall rate.

It was suggested during hearings on the Staggers Act that an amendment was desirable to require a railroad to provide its "best efficiencies" on demand from a shipper or a connecting water carrier. This would cure the situation in which, although a shipper may be offering an ample volume for a unit train, the railroad refuses to supply any service other than single car service at single car rates and such refusal has the effect of undermining competition. This is apparently the case for the vast tonnages of export coal.

This Committee recognized the problem at the time and incorporated safeguard language in each of the rate flexibility provisions. The language merely continued traditional safeguards against the undermining of rail-water competition and coordination.

The House felt a general safeguard qualifying every section would do the job and the Congress finally adopted Section 707, which reads as follows:

"SEC. 707. With respect to the relationship between water carriers and rail carriers, none of the amendments made by this Act shall be construed to make lawful (1) any competitive practice that is unfair, destructive, predatory, or otherwise undermines competition and that was unlawful on the effective date of this Act, or (2) any other competitive practice that is unfair, destructive, predatory, or otherwise undermines competition."

The conference report reinforced this statute with a comment as follows:

"The provision contained in this section, which qualifies each provision of each section of this Act, is designed to make clear that none of the provisions of the Act modifies existing law to make lawful a rate or practice that was unlawful on the day prior to enactment. Also the Conferees intend that this section allow water carriers to challenge practices that were unlawful as unfair, destructive, predatory, or otherwise undermined competition prior to enactment of this Act. In addition, of course, the Conferees do not intend to limit the rights of water carriers to exercise their rights and remedies under the provision of the Interstate Commerce Act as amended by the Staggers Act of 1980 regardless of whether those rights and remedies are related to practices which are unfair, destructive, predatory or otherwise undermine competition.

"The intent is that none of the amendments made by this Act is to be used to legitimize the undermining of rail-water competition. Railroad rates and practices that affect rail-water competition that are unfair, destructive, predatory, or otherwise undermine competition, and that were unlawful immediatly prior to enactment of this Act shall continue to be prohibited. Similarly, no change made by this Act makes lawful any other railroad rate or competitive practice that is unfair, destructive, predatory or otherwise undermines competiton."

The clear intent was certainly, as we understood it—and as the provision itself explicitly states—to qualify each and every relevant section of the Act so as to make sure that the provision preventing the undermining of rail-water competition would be paramount.

WTA is a party to a number of rule-making and other proceedings interpreting the Staggers Act. The trend of the Commission's actions so far with respect to water carrier rights under the Staggers Act seems to be in conflict with that clear intent. They either ignore the section entirely or argue in cases pending before the Court of Appeals that the provision has no such qualifying effect. If that position is upheld, of course, we will be back before this Committee for remedial legislation reinforcing the intent of the Congress as expressed in Section 707 to prevent the undermining of rail-water competition, thereby reaffirming that antitrust-type principles of competition govern rail-water relationships. We are in the process currently of taking advantage of such remedies as are available to us in the courts.

I note that a number of witnesses before this Committee, particularly those representing electric utilities, are concerned with the level of rail rates in the west. This Committee should be aware of a growing interest among farm groups, other shipper groups, state legislatures, commissioners of agriculture and others in scheduling a new Congressional investigation of land grant assets and mineral rights still held by four of the western railroads.

I am attaching to my testimony, as Appendix I,[1] a statement I recently prepared for the Western Coal Traffic League. It is a roundup of activities supporting a new Congressional investigation of land grant issues. The land grant question might not, at first glance, appear to be related to activities of the Commission under the Staggers Act. But the possibility of applying current government-provided land grant income in determinations of adequacy of revenues and earnings of railroads most certainly is relevant to problems shippers say they are having with the level of railroad rates.

The water carrier purpose in commissioning the first major study of the land grant question in some 35 years was to determine whether assets and current income from land grants should be included on the railroad side when comparisons are made between rail and barge subsidies. This is a question of major significance for "cost recovery" of government subsidies in transportation.

The study and WTA's subsequent intervention in the UP-WP-MP merger to urge, among other objectives, the return of land grant assets from the UP's affiliates to the railroad have created widespread new interest in the land grant question.

There are at least two major open questions on rail land grants.

[1] App. I has been retained in committee files.

The first is of fundamental importance. We find very much an open question needing Congressional resolution what obligation, if any, the land grant railroads have to use their land grant income to strengthen and sustain current railroad operations. The second issue is also of major consequence. To what extent have the land grant railroads breached their contract with the government by transferring land grant assets out of the railroad without adequate, or in some cases, any compensation?

The attached statement rounds up some of the background of the issues that are being raised in Congress and in the affected states on land grant issues.

Of particular interest is a "Legal Analysis of the Land Grants of the Northern Pacific Railroad," made public on October 19, 1981 by the Congressional Research Service of the Library of Congress.

The "discussion and summary" of this 40-page analysis is attached as Appendix II.[2]

The new study points out that, with respect to Burlington Northern's land grants, Congress could set out its interpretation of the grants and events and pursue any of several alternatives:

"(1) find that conditions of the land grants had been violated and revest title to some or all of the lands in the United States;

"(2) declare that the land grants were intended to subsidize the continued operation of the railroad and that any action on the part of the Burlington Northern that results in the segregation of the income of the land grant assets or their liquidated value from the operating expenses of the lines (or from the operating of the company's railroad functions in general) is unlawful, and provide time limits within which the company must make necessary adjustments; or

"(3) provide in some other way for a link between the income from the land assets or their liquidated value and the company's railroad functions, possibly by providing that certain percentages of such income or value must be shown by Burlington Northern as income and used in calculating their rates and demonstrating need for abandonment of various branches."

This, of course, would be precedent-setting for other land grant railroads.

This Committee may wish to join with other Committees in furthering investigation of the question or initiate its own investigation.

We appreciate this opportunity to appear before you today.

Statement of Coastal States Energy Company

INTRODUCTION

Coastal States Energy Company (Coastal) is a wholly-owned subsidiary of the Coastal Corporation, which is involved in the exploration, production, transportation, refining and marketing of energy products worldwide with revenues exceeding five billion dollars in 1980. Coastal's corporate offices are located at 9 Greenway Plaza, Houston, Texas 77046.

For the purposes of this hearing, we are primarily concerned with rail transportation pertinent to our interests in the (a) mining and production of coal, and (b) manufacture of fertilizers. A brief description of each of these two interests is provided below.

(a) *Coal.*—Coastal began purchasing coal properties in 1972 and now has investments in Utah, Kentucky, Illinois, Texas and Montana. In Utah, Coastal purchased the Southern Utah Fuel Company in 1973. This underground mine, located near Salina, Utah, today produces two million tons of coal annually and is the largest non-captive underground mine west of the Mississippi. Coastal also is engaged in opening three new mines in the northern WASATCH plateau field of central Utah near Scofield. Production is anticipated to commence in 1982 with the ultimate capacity at approximately five million tons per year. In Eastern Kentucky, Coastal purchased the McCoy Caney Coal Company near Phelps, Kentucky. Currently production and sales exceed one million tons per year; planned expansion will approximately double this amount by 1982.

In addition, Coastal has undeveloped reserves consisting of five properties located in Texas, Illinois and Montana. These properties are in various stages of predevelopment ranging from the preliminary exploration stage, such as the Montana Reserve, to property such as Coastal's large surface minable lignite reserves in Texas, which has been thoroughly core-drilled, evaluated and is awaiting market

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[2] App. II has been retained in committee files.

development. The combined total coal reserves of all these properties is currently approximately 430 million tons. From its current operations in coal, Coastal is generating approximately $30 million annually in rail freight payments.

(b) *Fertilizers.*—WYCON Chemical Company (WYCON) is a wholly owned subsidiary of the Coastal Corporation and part of Coastal States Energy Company. Wycon is located near Cheyenne, Wyoming, and produces nitrogen-based fertilizers, livestock feed supplements and liquid carbon dioxide. The Wycon plant represents a current investment value of approximately $33.3 million and produces in excess of 300,000 net tons of product annually. Wycon has been actively producing since 1965. Wycon operations generate approximately $5 million annually in rail frieght payments.

THE SIGNIFICANCE OF ACCESS TO ADEQUATE AND REASONABLE RAIL TRANSPORTATION TO OUR COMPANY

Coastal is greatly concerned with recent actions and initiatives regarding federal regulation of rail transportation. We are greatly dependent upon rail transportation to transport our products to market. Our products are bulk in nature and shipped in voluminous quantities. The average distance from point of production to the market exceeds 300 miles. In almost every instance, rail transportation represents the only viable means of transport available. Access to adequate and efficient rail transportation at just and reasonable prices is therefore critical to our business. It is estimated that our present operations generate in excess of $35 million annually in rail freight payments.

STATEMENT OF CONCERN

The Staggers Rail Act of 1980 ("Staggers Act"), Public Law 96-448, made substantial changes in rail carrier regulation by the Federal Government. Coastal followed the legislative debate leading to passage of the Staggers Act very closely and appreciate the fact that same was nothing less than a struggle. In the end, a delicate balance was achieved between the railroads and shippers.

Now, one year later, Coastal is seriously concerned in that the Interstate Commerce Commission (ICC) has had little regard for the captive shipper (i.e., those unable to bargain effectively with the railroads to secure reasonable rates), and provisions written by Congress into the Staggers Act for protection of the captive shipper are being misconstrued, ignored, and even flouted.

The Staggers Act balanced railroad revenue needs against continued protection of captive shippers from excessive rates. It is our position that now, just over one year from enactment of the Staggers Act, there are several actions and initiatives which severely threaten that balance, all to the preference of the railroads and detriment to the shippers. Of these, five actions represent the most potential source of irreparable harm to our company and respective industries and are here discussed, in brief.

Market dominance

No. 81-4257, et al., Western Coal Traffic League, et al., v. United States of America and Interstate Commerce Commission.

This action seeks judicial review before the Fifth U.S. Circuit Court of Appeals (New Orleans) of the ICC's decisions in Ex Parte No. 320 (Sub-No. 2), Market Dominance Determinations and Consideration of Product Competition; and Ex Parte No. 320, Rail Market Dominance; Removal of Existing Rule. These two decisions involve the "market dominance standards" to be employed by the ICC to determine whether it has jurisdiction to review the maximum reasonableness of rail transportation rates.

Under present law, a shipper complaining that a rail rate is unreasonably high, must first show the ICC that the rail traffic in question is subject to market dominance before arguing the issue of maximum reasonableness of the rate. It is clear that to preserve captive shipper protection provided both in the Railroad Revitilization and Regulatory Reform Act of 1976 (4R-Act) and the Staggers Act, it is essential that the definitions of rail market dominance be simple and adequate in scope.

The decisions served by the ICC seriously dilute the ability of a captive shipper to demonstrate that the rail traffic in question is subject to market dominance. If the issue decisions are permitted to stand, it is doubtful if jurisdiction could ever be established. We wish to strongly emphasize that this action pertains to all rail rates on all commodities and is, therefore, tremendous in scope.

The real question of the Staggers Act, whether competition in the marketplace produces reasonable rates so that the ICC need not get involved, has been complete-

ly ignored. If jurisdiction cannot be obtained over rates which a shipper can demonstrate are clearly in excess of any test of reasonableness applied in the past, either the market dominance test is wrong or the ICC is applying it in an erroneous manner. We believe Congress should clarify the law in this regard at the very earliest, and take action to see that where competition is not effective to produce reasonable rates, shippers should be accorded recourse to the ICC.

(ICC Notice of Proposed Exemption Ex Parte No. 346 (Sub-No. 7))

Railroad Exemption—Export Coal

The Norfolk and Western Railway Company (N & W) has petitioned the ICC to exempt export coal traffic handled by rail and moving through Altantic and Gulf ports from regulation. N & W contends that this traffic meets the criteria for exemption found in 49 U.S.C. 10505. The petition is supported by the Chessie System Railroads and the Family Lines Rail System.

The ICC issued a notice of proposed exemption served September 3, 1981, and published in the Federal Register on September 4, 1981, (46 FR 44529) seeking comments on the merits of exempting all export coal traffic from some or all regulations. The ICC has just recently established the comment period as 60 days from publication of notice in the Federal Register (published October 21, 1981, at 46 FR 51674).

The fact that the ICC did not dismiss the original petition outright, but actually broadened the scope and issued a notice of proposed exemption, which is now under formal consideration, represents a flagrant disregard of Congressional intent and meaning of the National Transportation Policy, the thrust of the Staggers Act, and transportation regulation history in general.

The contention that this traffic meets the criteria for exemption found in 49 U.S.C. 10505 is extremely questionable. This proceeding represents irreparable harm to our company and industry and will serve as a landmark precedent regarding the ICC's interpretation of the exemption provision at 49 U.S.C. 10505, as applied against rail captive traffic. The possible exemption of any coal traffic would set a dangerous precedent leading to the erosion of the captive shipper protection included in the Staggers Act.

The National Coal Association, Inc. completed a 1979 study of captive coal shipment by rail. That study indicated that: (a) Of all the market types of rail transportation of coal examined (utility, steel, industrial, exports), the export market was shown to have the highest percent captivity to all—93 percent captive, and (b) the next best transportation alternative to rail would cost shippers almost 300 percent of the average rail cost.

The transportation of coal by rail has historically been recognized as a classic example of monopolization. The need for protection of captive shippers from rail monopolization by regulation has also been historically recognized—that is, until now. The original Interstate Commerce Act of 1887 was enacted to prevent the very types of abuses that, we feel, would again be prevalent if issue traffic is exempted.

Any contention that issue traffic meets the criteria provided at 49 U.S.C. 10505 is in direct conflict with the Staggers Act and National Transportation Policy. Any balance that we thought was attained in the Staggers Act between captive shippers and railroad economic needs would be completely destroyed.

The railroads would again be placed in a position to extract monopoly rents from captive shippers.

Shippers would be forced to pay the price demanded while deprived of any effective administrative or judicial recourse.

Shippers' ability to negotiate contracts with rail carriers will be seriously impaired as, without regulatory constraints, there will be no incentive for the carriers to negotiate contracts.

Common carrier liability could be seriously impaired or completely eliminated and shippers would have no assurance they could get their product to market, regardless of price.

The attraction necessary to achieve private sector investment in the affected industries would be seriously diminished.

We do not feel Congress intended the exemption provision at 49 U.S.C. 10505 to be interpreted or applied as the ICC is now proposing. The Staggers Act clearly recognized the need for captive shipper protection from excessive rates. We believe Congress should clarify this intent and purpose for the ICC before all is obliviated by administrative fiat.

88-534 O - 82 - 11

(ICC Notice of Proposed Guidelines Ex Parte No. 347 (Sub-No. 1))

Coal rate guidelines—nationwide

This proceeding has as its purpose the establishment of guidelines to be used in the determination of maximum reasonable rail rates on coal, once the issue of market dominance has been established. In May of 1978, the *ICC instituted* a proceeding (Ex Parte No. 347) to establish rate guidelines for rail transportation of western coal. After receiving public comment, the ICC, pursuant to notice dated November 18, 1980, decided not to issue an order, but rather to broaden the proceeding to consider rail coal rate guidelines nationwide [Ex Parte No. 347 (Sub-No. 1)]. Comments in this proceeding were solicited and received in May of 1981. Since that time, a final decision by the ICC has been pending, but no formal action has been taken.

Two issues fundamental to this proceeding are in direct conflict with Congressional intent as expressed in the Staggers Act.

(1) The ICC proposes to use a ton/ton mile method for allocating fixed costs instead of the ratio method previously employed. The proposed methodology is clearly prejudicial against heavy-loading, long-haul traffic (i.e., rail captive traffic). This action would serve to jeopardize the balance provided in the Staggers Act between rail captive shippers and railroad economic needs.

(2) The respondent rail carriers have been permitted to broaden the issue proceeding further by proposing the use of value of service pricing rather than the cost of service methodology currently employed in the determination of the levels of maximum rate reasonableness. This proposal is in direct conflict with the emphasis placed on cost determinations provided in the Staggers Act (i.e., jurisdictional threshold, revenue adequacy determinations, surcharge applications, automatic cost-based increases, etc.). Further, this proposal would serve to further jeopardize the above-mentioned balance between rail carriers and captive shippers in that same raises serious unanswered questions of economic efficiency and fairness.

We commend the ICC for giving special attention to maximum reasonable coal transportation rates. However, we feel the ICC has failed to recognize the thrust and Congressional intent of the Staggers Act and feel that Congress should so advise same prior to any further ICC action regarding issue proceeding.

Railroad abandonments

The denial ratio in railroad abandonment applications has been dramatically low. In fact, the ICC recently ended a 25 month period, beginning August 1, 1979, in which no abandonments were denied (decision served September 16, 1981, in AB-1, Sub 117F, Chicago & North Western Transportation Co., Abandonment Between Elgin and Crystal Lake, Ill., in Kane and McHenry Counties, Ill.).

The standards employed by the ICC in abandonment proceedings were examined, but relatively unchanged by the Staggers Rail Act. Meanwhile, the ICC has allowed for the inclusion of opportunity costs as a factor worthy of consideration in these proceedings (see Abandonment of Railroad Lines—Use of Opportunity Cost, 360 ICC 571; affirmed at 642 F. 2d 208).

The term "opportunity cost" used here refers to consideration (in favor of abandonment) of the fact that a railroad company can earn elsewhere a greater return on its investment in land and track materials than it can earn by continued rail operation of the line at issue. The greater return used in determining opportunity cost may be achieved in non-railroad use. Under that concept, railroads are encouraged to abandon many profitable lines.

We feel that a policy of encouraging disinvestment in railroad branch lines is highly questionable as a matter of national transportation policy. Further, as this policy serves to decrease competition, it is therefore in conflict with the Staggers Rail Act and the National Transportation Policy.

We request Congress to reassess the regulatory criteria applied to abandonment proceedings to determine (a) if the ICC is applying same fairly and impartially and (b) if same reflect Congressional intent and serve to further the National Transportation Policy.

Availability of accurate railroad cost data

The emphasis placed on cost of service determinations was extremely heightened by the Staggers Act (i.e., jurisdictional thresholds, revenue adequacy determinations, surcharge applications, automatic cost-based increases, etc.). Shipper access to accurate railroad cost data is necessary to maintain the balance provided in Staggers Act between carriers and shippers.

The Staggers Act provided a new framework for continuing the development of the railroad cost determination process. Section 302(a) of the Staggers Act estab-

lished a "Railroad Accounting Principles Board" (Board), and provided that same shall be within and responsible to the legislative branch of the Federal Government (49 U.S.C. 11161). At 49 U.S.C. 11162, it is provided that within two years of the effective date of the Staggers Act (October 14, 1980), the Board "shall establish for rail carriers . . . principles governing the determination of economically accurate railroad costs directly and indirectly associated with particular movements of goods. . ."

The above-cited provisions were a part of the compromise offered to shippers in return for their support of the Staggers Act. It is doubtful if the Staggers Act could have been passed without this provision. However, these provisions have not yet been implemented. No one has been appointed to the Board. The Board is not functioning because Congress has not provided the money, although appropriations were authorized by Section 302(a) of the Staggers Act.

The Railroad Revitilization and Regulatory Reform Act of 1976 (4-R Act) required the ICC to develop a new Uniform System of Accounts (USOA) for the railroads, and in the process it started work on a new Uniform Rail Costing System (URCS) to replace Rail Form A. Both USOA and URCS were developed by outside "contractors" employed by the ICC, who have major committeements to the rail industry. The effect of USOA and URCS substantially arises the carriers' variable costs of handling heavy-loading, long-haul, bulk traffic (i.e., captive traffic).

We feel that URCS should not be implemented until the Board is activated (with shipper representation, as provided) and allowed the opportunity to thoroughly review and determine the reliability and accuracy of same. Further, USOA should be so reviewed by the Board at the very earliest practicable date.

Coastal is strongly convinced that it is essential for the protection of the interests of captive shippers that the Railroad Accounting Principles Board be established as a functioning organization without further delay and that shippers should have adequate representation thereon.

CONCLUSION

Coastal recommends that a series of Congressional oversight hearings be held on all matters of significance developed in this hearing as expeditiously as practical.

We commend Congress on the resultant legislation enacted by the Staggers Act in that a balance was achieved between captive shippers and railroad economic needs. Coastal feels that the problems discussed herein could be cured, and all parties spared extremely time consuming and expensive litigation, if Congress would clarify those parts of the Staggers Act which have given the most trouble, indicating to the ICC that its duty is not to make policy on its own, but to carry out the policy of Congress as expressed in the Staggers Act.

Statement of the Florida Phosphate Council, Inc.

The Florida Phosphate Council, Inc., is a trade association representing the major phosphate mining and chemical companies with operations in Florida. The phosphate industry ships millions of tons annually of bulk phosphate rock and phosphate chemcials. Transportation is almost solely by railroad. All of the plants and facilities of the member companies in central Florida are served by only one railroad which has a monopoly over the industry's transportation needs.

These comments are limited to the implementation of the Staggers Rail Act by the Interstate Commerce Commission. Of particualar concern to the Florida phosphate industry is the Interstate Commerce Commission interpretation of the statutory concept of "market dominance."

Transportation in the phosphate mining area of central Florida, known as "Bone Valley", is unique. It is one of the most concentrated areas for bulk rail movement in the nation. In 1980, approximately 50 million tons, or 88 percent of the total tonnage of phosphate rock and phosphate chemicals, moved via the Seaboard Coast Line Railroad within this area and to the Tampa ports. An additional 7 million tons moved by motor carrier, however, this mode has reached its saturation point. The greatest portion of all of this traffic is moved within a radius of only 35 miles. The rail movement is almost exclusively made in trainload lots with practically all of the companies performing their own switching operations with their own equipment and tendering shipments in multi-car or trainload lots on a "hook and haul" basis. It is physically and logistically infeasible to handle this traffic by truck and would be far beyond the capacity of the present highway system in this area. In fact, prohibitions on additional truck hauling have been imposed by some of the local governments in the mining counties.

As captive shippers to a monopolistic railroad, the phosphate industry believes its interests would be adversely affected bythe Interstate Commerce Commission's decision, served July 8, 1981, in Ex Parte No. 320 (Sub-No. 2), Rail Market Dominance, 365 ICC 116. Ex Parte No. 320 replaces the reasonable presumptions of market dominance contained in the 4R Act of 1976 and the Staggers Rail Act of 1980, i.e., costs, market share and substantial investment, with new guidelines based on evidence of geographic and product competition. What this means to the phosphate industry is that phosphate rock shipped from the mine to an intermediate chemical plant where it is processed, and from the chemical plant, it is shipped out of state, would not be "market dominant" if there was competition anywhere in the transportation, even though the first leg of the shipment from the mine to the plant was served by only one railroad and other modes of transportation were not available. If the railroad seeks a finding that shipments of phosphate rock are market dominant under these guidelines and identifies where such competition either geographic or product exists, the burden is on the shippers to prove that the competition is not effective to counterbalance the monopoly in the first phase of the shipment. This would be extremely difficult because of the necessity of a complete record of complex factors affecting transportation competition which as the Interstate Commerce Commission acknowledges are numerous and varied (365 ICC at 120) and are only partially available to shippers.

The Florida Phosphate Council, Inc., does not believe Congress intended to legislate that geographic and product competition should enter into determinations of market dominance. This view has the support of well-reasoned and documented authority. (See, Eckhardt, Market Dominance in the Staggers Act, 48 I.C.C.P.J. 662). Without a proving of market dominance, the shippers' door to seeking relief from the Interstate Commerce Commission on unreasonable rates is closed, and the railroad is free to charge rates as high as the traffic will bear.

Predatory pricing with inflationary rates by the railroad on the transportation of the phosphate industry's products must be passed on to the consumer, the nation's farmers, and can only result in adding to inflation, and in the case of international shipments, adversely effect the balance of payments.

If Congress is to preserve and carry out the goals of the Staggers Rail Act, it should preserve the mandate "to provide a regulatory process that balances the needs of carriers, shippers, and the public". At the moment, the Interstate Commerce Commission, evidenced by its rules on market dominance seems interested only in the revenue adequacy of the railroads. This subcommittee should carefully review the Interstate Commerce Commission's actions in this area and take whatever steps are appropriate, including legislation, to remedy the problem.

The Florida Phosphate Council, Inc., believes the Commission should vacate its order of July 8, 1981, in its entirety and substitute by rule, standards and procedures which carry forward the intent of Congress expressed in Section 202 of the 4R Act and Section 202 of the Staggers Act. If it does not, the Florida Phosphate Council, Inc., believes Congress should address the issue.

Statement of William C. Hennessy, Commissioner of Transportation, New York State Department of Transportation

During the latter portion of 1979 and the first half of 1980, the New York State Department of Transportation closely followed the development of the federal rail regulation legislation that eventually evolved into the Staggers Rail Act of 1980. We participated freely in this development process and took advantage of numerous opportunities to inform the members of the relevant committees—particularly our own representatives in the Congress—of our assessment of various aspects of the proposed legislation and of the ways in which we felt the legislation could be improved. When the Rail Act eventually came to fruition, we felt that it represented a well thought-out approach to the problem of deregulating the rail industry, an approach that would benefit not only the industry itself, but also it users.

While the Rail Act was signed into law a year ago, implementation of many of its provisions has moved along very slowly. In addition, the impacts of the Act were very quickly overshadowed by the issues raised during the development of the recently enacted Northeast Rail Service Act of 1981. Nonetheless, a sufficient number of actions have been taken under the Staggers Act to allow us to draw several conclusions regarding its likely impacts in New York State. I would like to take note of two areas that we feel are of concern, the implementation of the joint rate surcharge/cancellation mechanism established by Section 217 of the Staggers Act; and, the Feeder Railroad Development Program created by Section 401.

JOINT RATE SURCHARGE/CANCELLATION

Basically, our concern in this area arises from the fact that the freedom to surcharge or cancel joint rates presently participated in by Conrail, the Long Island Railroad and/or the New York Dock is very rapidly destroying the rate parity long established in the New York City area.

Over the years, the Long Island Rail Road and New York Dock/BEDT backed by prior ICC decisions and policy, have maintained a rate structure such that total rates to and from points in Brooklyn and in that part of Long Island within the Metropolitan New York area are, for the most part, equal to those rates to and from points on Conrail within the Metropolitan New York area. Thus, the freight users served by the LIRR and NYD/BEDT within the Metropolitan area have not been placed at a competitive disadvantage vis-a-vis those on Conrail's lines within the Metropolitan New York area. This situation is referred to as rate parity within the New York, New York rate group. Recent actions taken by Conrail under Section 217 of the Staggers Act, however, have had the effect of undermining this historical practice of region-wide rate parities.

The provisions of Section 217 which have had the largest impact are those which permit a carrier which fails to recover at least 110% of its variable cost by way of its divison of a joint rate to either (a) impose a surcharge which will bring it up to a maximum of 110% of its variable cost; or (b) cancel the joint rate and publish its own rate for its portion of the move, thus leaving all other carriers involved in the move to do the same.

As an example of the effects these provisions have had, I would like to cite the situation now facing the LIRR. All interline traffic handled by LIRR passes over the lines of Conrail and is recieved at a single interchange point at Fresh Pond, Queens. Thus, the LIRR (and NYD/BEDT) is—in a real sense—a "captive" of Conrail: any joint rate adjustment action Conrail takes on LIRR traffic must impact the LIRR because the latter has no alternate connections to turn to.

Conrail has already imposed a surcharge on pulpboard and wrapping paper which has had the effect of raising the per car freight cost by about $250 per car to Long Island freight users. Since the surcharge dos not apply to traffic destined for points on Conrail, this has destroyed the rate parity on this commodity in the Metropolitan New York area.

Furthermore, again under the provisions of the Staggers Act, Conrail has cancelled joint rates on certain commodities and published its own rates for its portion of the haul on these commodities. The problem presented to LIRR in such joint rate cancellations is that when Conrail's rate is added to that of the other carriers involved in the move, the total cost to bring a car to the interchange point with the LIRR can, in may instances, approach or even exceed the previous entire rate to deliver the car to a customer on Long Island. Thus, if LIRR were to publish its own rate at a level designed to recapture the previous per car earnings, there will be a steep cost increase to the shipper leading to disruption of rate parity. This, in turn, would put the Long Island shipper at a distinct economic disadvantage relative to his competitor—precisely the event that the rate parity approach was designed to preclude.

Similarly, on June 9 Conrail filed a tariff with the ICC changing the rates for shipment of grains and grain products from single-factor joint rates to combination rates. By tariff supplements—effective August 15 of this year—Conrail also proposed to withdraw from participating in existing joint rates for the transportation of grains and grain products. As a result of these actions, all Conrail rates to destinations within the New York rate group will be lower than the joint rate (now cancelled) applicable to destinations on NYD and BEDT. Since Conrail is the only connecting line-haul railroad over which freight has moved to or from NYD and BEDT and is the only Class I rail carrier serving stations in the Port of New York, the effect of Conrail's actions is: (a) to offer rates on grain and grain products to points served by Conrail alone in the City and Port of New York that are lower than rates on grain and grain products shipped to points served by NYD and BEDT in the City and Port of New York; (b) to divert traffic from NYD and BEDT to Conrail; (c) to disrupt current rate equalization within the Metropolitan New York area; (d) to enhance Conrail's dominance of rail traffic in the existing market to, from and within the Port of New York and the New York rate basis; (e) place an unwarranted competitive burden upon NYD and BEDT and their customers; and, (f) impair NYD's and BEDT's ability to earn an adequate return on their investments. Even though such predatory action is explicityly forbidden by the Class III protective provisions of Section 217, Conrail's "restructured" rates were allowed to become effective and will remain in effect pending the outcome of an ICC investigation.

Section 217—or, more accurately, the manner in which Conrail has chosen to implement it—has been the source of other problems, as well. For example, Conrail has apparently decided to use the origin-termination surcharge mechanism provided by this Section as a device to address problems that are basically of a commodity nature. Such problems be addressed on a commodity basis through tariff revisions and in conjunction with connection carriers. They should not be the subject of selective surcharge impositions. A recent instance of such an action involves the Tonawanda Industrial Track and its two major shippers: R.T. Jones Lumber and International Filler. The use of this mechanism in instances such as this is, in our assessment, discriminatory.

A final point to be made relative to Section 217 is that concerning Conrail's provision of data to shippers and connecting carriers involved in a given surcharge/cancellation action. In general, Conrail has refused to provide detailed backup data supporting its imposition of surcharges, especially those involving origin/termination movements. The 33-day response time allowed in the ICC process is too short in most cases to put together the necessary background data if it has to be obtained from a variety of shippers and other users and to generate from that data an accurate set of independent cost estimates. Many loadings are not prepaid; thus, the necessary costing records are not readily available. If the "provision of data" process is to be a meaningful exercise, we believe that the ICC will have to *require* the carrier initiating the surcharge or cancellation to disclose the basic costing data used in calculating the surcharge or as the basis for the cancellation. Failing this, the ICC must revise the timing of their process to allow at least 60 days for the protestant to develop an independent set of costing estimates.

FEEDER RAILROAD DEVELOPMENT PROGRAM

Insofar as the Feeder Railroad Development Program is concerned, I would like to reiterate our support of its objectives and of the process establishing it in Section 401. We are very disappointed, however, to find that Congress has again decided not to provide any funding to assist in implementing this program.

This lack of funding has rendered the program developed by Congress to ease the impacts of the pricing and abandonment freedoms granted carriers by the Staggers Act upon local shippers and communities almost totally ineffective. While this situation is no doubt an inadvertent result of Congress' desire to put increased emphasis on alternative funding mechanisms (e.g., the 4R Act's Section 511 obligation guarantee program) that are intended to achieve much the same objectives as the preference share program, it has nonetheless thwarted the intent of the Feeder Railroad Program.

When this lack of effectiveness of the Program's part is combined with the additional "expedited abandonment" freedoms granted Conrail under Section 1156 of the Northeast Rail Service Act of 1981, we believe that the balanced approach the Congress attempted to take in addressing the concerns of shippers and communities, on the one hand, and those of Conrail, on the other, will be badly upset. The Feeder Railroad Program offers affected shippers and communities an opportunity to deal with the problems presented by a Conrail branchline operation of a marginal or uneconomic nature before service or physical condition deteriorate further and before abandonment ("expedited" or otherwise) becomes necessary. It allows such business and community interests to preserve their rail services by taking over operation of the line from Conrail, thereby relieving Conrail (and, indirectly, the federal government) of involvement in a non-compensatory operation. To seriously inhibit this program from effecting its goals due to a lack of funding would appear to be inconsistent with Congress' intent relative to the program, as expressed in the Staggers Act.

Section 1156 of the Northeast Rail Service Act of 1981 provides for the sale of lines abandoned by Conrail under this Section to another party at a cost of 75 percent of the net liquidation value of the line (this value is to be determined by the ICC). The immediate disposition of any funds generated by such sales is not specified in the Act. It is our position that, as the effected lines were purchased for Conrail with public monies and are, in a sense, public properties, all proceeds should accrue to those who paid for the properties—the public treasury. Thus, the funds produced by the sale of lines abandoned by Conrail in its initial use of Section 1156's preogatives could potentially be utilized to make loans to entities wishing to secure the services on not-yet-abandoned lines under the Feeder Railroad Program—or to guarantee such loans made in the private sector—hence, eliminating or at least alleviating the negative impacts of a subsequent series of Section 1156 abandonments. I have appended a copy of our proposal on this matter to this statement.

Thus, it appears that a funding mechanism can be developed to support the Program, a mechanism that does not require additional federal funds or appropriations actions. This mechanism can be implemented within existing legislation and will not have any direct budget implications. The proceeds realized from the sale of Conrail properties—properties for which Conrail has never paid and never will—under Section 1156 should be dedicated on a state-by-state basis to the implementation of the Feeder Railroad Program. It is our firm belief that the proceeds from the initial round of such sales will enable shipper groups, local community agencies, Class III railroad operators, and other entities to develop solutions to the problems of non-compensatory branchlines and threatened service discontinuances that will ease the necessity for further loss of rail service in subsequent years. Certainly, this would be preferable to the continued loss of our branchline services and to the disruptive effects such losses have upon those businesses and communities economically dependent upon these services.

NORTHEAST RAIL SERVICES ACT OF 1981

As I noted earlier, a great deal of the attention due the Staggers Act and its impacts was diverted by the attempts to develop new legislation dealing with Conrail. Because this legislation so quickly overshadowed the Staggers Act and even negated portions of it so far as Conrail is concerned, I think that it would be appropriate to mention a few of the issues the new "Conrail bill" raises relative to our carriers and shippers. In general, we feel that the Northeast Rail Services Act of 1981 represents a rather hasty attempt to set a timetable for a federal withdrawal from the business of railroading. We certainly have no argument with that objective; in fact, we have long been in favor of such action. We felt, however, that the Staggers Act should have been given a chance to work and that there was no need for a series of special dispensations granting Conrail a number of operational and economic advantages over its competitors. Yet, this seems to be precisely what NERSA will result in.

For example, the provision exempting Conrail from liability for all state-level taxation is clearly inequitable; it may even be unconstitutional. While this action will deprive New York State of some $12 million to $14 million in annual revenues, this is not the most significant impact of this action. Of greater importance is the inhibiting effect it will have upon the re-introduction of rail competition into our State—and into the Northeast as a whole. We simply cannot understand why Conrail should be accorded such a favored status.

In a similar fashion, we could see no need for—and vigrously opposed—the establishment of a specially designed "expedited abandonment" process for Conrail's use. Nonetheless, NERSA provides such a process—even though the Staggers Act contains a considerably shortened, well-constructed abandonment process that is still, to all intents and purposes, untried. The NERSA process allows Conrail to abandon virtually any line it chooses, upon 90 days' notice. While this new process does provide for "offers of financial assistance," this is of little practical value to those wishing to preserve the threatened rail service. Ninety days is simply too short a period within which to put together a sound, well-developed offer of financial assistance. Conrail has already gone beyond this concession by its decision not to make use of the System Diagram Map to forewarn of its plans to abandon lines. I don't believe it was Congress' intent to leave this as Conrail's option—ICC should take a stand here. This new abandonment process will lead to a rapid-fire series of large scale abandonment applications within the very near future, causing considerable havoc to the best interests of the businesses and citizens of this State, as well as negating many of the efforts and expense the State went to in its quest to ensure the continuation of our essential rail services. We view this new process as a serious blow to the economy of this State and of the Northeast as a whole.

To complement the perogatives granted Conrail by this new abandonment process, NERSA would seem to provide Conrail with an opportunity to actually prevent or preclude the establishment of an alternate operator on a line Conrail itself no longer wishes to operate. Conrail can conceivably achieve this result by initially establishing an unreasonably high estimate of a given line's net liquidation value, by being dilatory in providing basic costing data to parties interested in acquiring the line and establishing their own operations over it, by trying to stop the purchase of only those lines (or line segments) a potential acquirer is interested in, and so on. Section 1156 does not prevent such machinations, nor does it even address them. Unfortunately, the recently issued ICC "policy" on this subject would seem to do little to prevent such abuses, either. If left to its own devices, Conrail can be expected to act on the basis of its own short-term interests in its efforts to attain the "profitability" standard set for it by NERSA, regardless of the detrimental longer-

term impacts these actions will have upon the interests of the businesses and citizens of this State and, indeed, of the entire Northeast. We find it difficult to believe that this is the result Congress intended NERSA to have. We would hope that the Congress will recognize these problems and that it will take such steps as are necessary to prevent them before they precipitate an even greater economic crisis in our part of the country than the one we now face.

In closing, I would like to thank the members of this Subcommittee for offering us this opportunity of expressing our thoughts on, and assessments of, the Staggers Rail Act of 1980 and of entering these assessments into the public record.

FUNDING MECHANISM FOR THE FEEDER RAILROAD DEVELOPMENT PROGRAM

Background

Section 401 of the Staggers Rail Act of 1980 established the Feeder Railroad Development Program. It was the purpose of this Program to provide shipper groups, communities and other financially responsible entities with an alternative to inadequate rail service or abandonment, and with an opportunity to preserve feeder lines and the service they provide prior to the total physical downgrading of such lines.

In order to assist in the effective implementation of the Program, Section 405 of the Staggers Act required that no less than five percent of any monies appropriated for redeemable preference share financing (under Section 505 of the 4R Act) be dedicated to the Feeder Railroad Program. Although the Staggers Act authorized some $700 million in additional funds for the redeemable preference share program (hence, some $35 million for the Feeder Railroad Program) no monies were appropriated for this purpose during federal fiscal year 1981. Similarly, no monies have been appropriated for the redeemable preference share program (and, therefore, the Feeder Railroad Program) in the recently passed House appropriation bill for federal fiscal year 1982.

The problem

This lack of funding has rendered the program developed by Congress to ease the impacts of the pricing and abandonment freedoms granted carriers by the Staggers Act upon local shippers and communities almost totally ineffective. While this situation is no doubt an inadvertent result of Congress' desire to put increased emphasis on alternative funding mechanisms (e.g., the 4R Act's Section 511 obligation guarantee program) that are intended to achieve much the same objectives as the preference share program, it has nonetheless thwarted the intent of the Feeder Railroad Program.

When this lack of effectiveness on the Program's part is combined with the additional "expedited abandonment" freedoms granted Conrail under Section 1156 of the Northeast Rail Service Act of 1981, we believe that the balanced approach the Congress attempted to take in addressing the concerns of shippers and communities, on the one hand, and those of Conrail, on the other, will be badly upset. The Feeder Railroad Program offers affected shippers and communities an opportunity to deal with the problems presented by a Conrail branchline operation of a marginal or uneconomic nature *before* service or physical condition deteriorate further and *before* abandonment ("expedited" or otherwise) becomes necessary. It allows such business and community interests to preserve their rail services by taking over operation of the line from Conrail, thereby relieving Conrail (and, indirectly, the federal government) of involvment in a noncompensatory operation. To seriously inhibit this program from effecting its goals due to a lack of funding would appear to be inconsistent with Congress' intent relative to the program, as expressed in the Staggers Act.

A proposed solution

Section 1156 of the Northeast Rail Service Act of 1981 provides for the sale of lines abandoned by Conrail under this Section to another party at a cost of 75 percent of the net liquidation value of the line (this value is to be determined by the ICC). The immediate disposition of any funds generated by such sales is not specified in the Act; new paragraph 308(e)(4) of the 3R Act—created by Section 1156—suggests, however, that these funds may be held in an "escrow" type of account for a period of as long as five years. Thus, the funds produced by the sale of lines abandoned by Conrail in its initial use of Section 1156's perogatives could potentially be utilized to guarantee loans made to entities wishing to purchase not-yet abandoned lines under the Feeder Railroad Program—hence, eliminating or at least alleviating the negative impacts of a subsequent series of Section 1156 abandonments.

As the Feeder Railroad Development Program is a loan guarantee program—*not* a grant program—additional federal monies are not required; thus, a change to the current federal fiscal year 1982 appropriation bills is not required. The funds generated by the sale of lines abandoned under Section 1156 should be sufficient to provide for an effective level of loan guarantees over the course of the next two or three years (a reasonable estimate of the NLV for the average low-density line is about $30,000 per mile; 75 percent of this is $22,500 per mile. Conrail is contemplating abandonment of nearly 2,500 miles of line; if only one-third of this is sold, it will generate some $25 million to support the loan guarantees needed to implement the Feeder Railroad Program).

Thus, it appears that a funding mechanism can be developed to support the Program, a mechanism that does not require additional federal funds or appropriations actions. This mechanism can be implemented within existing legislation and will not have any direct budget implications. The proceeds realized from the sale of Conrail properties—properties for which Conrail has never paid and never will—under Section 1156 should be dedicated on a state-by-state basis to the implementation of the Feeder Railroad Program. It is our firm belief that the proceeds from the initial round of such sales will enable shipper groups, local community agencies, Class III railroad operators, and other entities to develop solutions to the problems of non-compensatory branchlines and threatened service discontinuances that will ease the necessity for further loss of rail service in subsequent years. Certainly, this would be preferable to the continued loss of our branchline services and to the disruptive effects such losses have upon those businesses and communities economically dependent upon these services.

Statement of Kent Jones, North Dakota Commissioner of Agriculture

The purpose of the Stagger Act was to alleviate the financial plight of the railroads. The Act was an attempt to reduce governmetal regulations to enable the railroads to more effectively compete with other modes of transportation. Government regulations had stifled the ability of the railroads to compete in the 20th Century, and the Stagger Act was enacted to put the railroads on a more business-like footing. The Act, however, has created unforeseen difficulties for rural communities.

In order to allow railroads to operate with more managerial flexibility, the Stagger Act shortened the time frame within which the railroads could legitimately abandon selected lines. Although the Act did not make changes in the substantive abandonment requirements, the time limits were considerably shortened.

The purpose of this change was to expedite abandonment procedures by specifically setting forth time periods within which the Interstate Commerce Commission must act upon abandonment applications. Although the time limitations are harmful, they are not in and of themselves the major shortcoming of this legislation.

Prior to the enactment of the Stagger Act the I.C.C. was required, upon protest, to begin an investigation to determine the disposition of an abandoment application. This was mandated by statute. The statutory language of the new Act, however, simply states that if a protest is filed, the I.C.C. is merely required to determine "whether the investigation is needed" within 45 days after the abandonment application is filed. It is this portion of the Act which is particularly unfair to those who wish to retain rail service to their businesses and communities. The Stagger Act allows the I.C.C. the discretion, even amidst the protests of its constituents, to irrevocably cut off rail service to a community within a month and a half after the filing of an application to abandon. Historically, the successful protestation of an abandonment application was difficult; the Stagger Act serves now to make it virtually impossible. Although the underlying emphasis on de-regulation is sound and practical, the unforeseen difficulties surrounding the abuse of abandonment procedures need to be rectified.

The Stagger Act was an attempt to help financially troubled railroads. Burlington Northern is not such a railroad. Its earnings and holdings have increased every year, and it possesses literally billions and billions of dollars in land grant assests. It operates over 2,000 miles of branch lines in trackage in North Dakota. Most of these lines serve grain elevators in small rural communities. The current abandonment procedures in the Stagger Act allows Burlington Northern to escape its legal obligation to provide rail service to these communities. Burlington Northern's superior resources, coupled with liberal abandonment regulations, serve to deny those people along branch lines any meaningful response to an application for abandonment. Long-term planning allows Burlington Northern time to gather a convincing case for abandonment, while its unwary consumers wake up one morning to find that

their community no longer fits into Burlington Northern's plans for the future. Last summer's events bear witness to this proposition. The number of miles in category #1 in BN's rail design has created a sense of panic among elevator operators and communities where large investments have been made in new or improved facilities. Time is needed for these communities to come to grips with what to do with their grain and how to adapt their local elevator usage to a changed transportation scheme.

North Dakota is an agricultural state. Over 70 per cent of our gross income is derived from the farming sector. In recent years we have sought to increase our influence in the markets by investing in cleaning plants, processing plants, and packaging plants. The investments in these businesses stand as a constant reminder of the confidence and faith these people have in their towns, their state, and their profession. Many of these new businesses are located on branch lines. To retain the relaxed abandonment procedures of the Stagger Act, which allow Burlington Northern to abuse its superior bargaining position, is to work an injustice of unspeakable proportions on the people of North Dakota.

The legislative history of the Stagger Act denotes the fact that little consideration was given to abandonment procedures. We would like Congress to now reconsider this portion of the Act. To fail to do so would be unconscionable. Burlington Northern has attempted to abandon the people of North Dakota; we would hope that Congress does not follow suit.

Statement of George Carl Pezold, Executive Director-General Counsel, on Behalf of Freight Users Association of Long Island, Inc.

INTRODUCTION

My name is George Carl Pezold and I am Executive Director and General Counsel of the Freight Users Association of Long Island, Inc., with offices at 120 Main Street, Huntington, New York. I make this statement on behalf of the rail freight shippers and receivers who use and are served by the Long Island Rail Road.

I am a practicing attorney, specializing in transportation law, and hold a J.D. degree from New York University School of Law (1962) and an M.E. degree from Stevens Institute of Technology (1959). In the course of my practice, I have represented numerous rail shippers and receivers, associations such as Freight Users Association of Long Island, Northeastern Retail Lumbermens Association, National Lumber & Building Materials Dealers Association, Walkill Valley Rail Users Association, municipalities such as the County of Orange, New York, all in connection with proceedings before the Interstate Commerce Commission or the courts relating to rail freight matters.

The Freight Users Association of Long Island, Inc. ("FUA"), is a not-for-profit corporation organized under the laws of the State of New York, with principal offices in the Town of Huntington, County of Suffolk, State of New York. The membership of FUA is comprised principally of shippers and consignees of rail freight in Nassau, Suffolk, Brooklyn and Queens. The Association has acted as the principal spokesman and representative of Long Island's freight users since 1970 with respect to rail freight service, rates, tariffs and related matters. Our current membership stands at 78 companies, which account for a substantial portion of the rail freight moving to or from the region. See Membership List, App. A.

BACKGROUND

For a century, rail freight rates between western and southern origins and northeastern destinations have recognized the concept of a New York "rate group". All points within this region, which encompasses New York City, parts of northern New Jersey, Long Island, Westchester, etc., have enjoyed rate parity with one another. Although the practice originated with the railroads themselves, it became well established in the decisional law of the ICC and its interpretation of the Interstate Commerce Act. See, e.g., *Eastern Class Rate Investigation,* 164 ICC 314, 425 et seq (1930).

As recently as 1978, the ICC reaffirmed that it would be an unlawful practice and a violation of the statutory prohibition against discrimination to charge a rail receiver on Long Island a higher rate than his nearby competitors in the New York metropolitan region. *S & K Farms, Inc. and Freight Users Association of Long Island, Inc. v. The Long Island Rail Road Company, et al.,* 357 ICC 562 (1978);

appeal dismissed as moot. — F.2d — (9th Cir. 1980). A copy of the ICC's decision in the *S. & K. Farms* case is annexed. App. B.[1]

The Staggers Rail Act of 1980, however, brought about sweeping changes which have disrupted these traditional rate relationships.

THE STAGGERS ACT

During the maneuverings immediately prior to the enactment of the Staggers Rail Act of 1980 (P.L. 96-448, signed by President Carter on October 14, 1980), ConRail was able to insert language into the legislation which became "Section 217—Compensatory Joint Rate Relief". 49 U.S.C. 10705a. (NOTE: Similar language in prior versions had been knocked down by the Eckert-Rahall Amendment package, approved by the House in July of 1980; however, Rep. Florio pulled the bill off the floor at that time.)

Section 217 of the Staggers Act was intended to give ConRail a shortcut way to increase its revenues without obtaining the concurrence of its connecting carriers or the approval of the ICC.

It allowed ConRail to impose, for its own account, a unilateral surcharge on any traffic which showed a "revenue-to-variable-cost ratio" less than 110 percent. It also allowed ConRail to cancel joint rates applicable to any through route where the revenue earned is less than 110 percent of the variable cost of providing service over the route.

These new statutory provisions were unprecedented. In fact, earlier attempts by ConRail to impose unilateral surcharges on certain commodities had been found unlawful. See, e.g., I & S Docket No. 9222, *ConRail Surcharge on Pulpboard*, 4/22/80. Similarly, attempts to cancel joint rates had been prevented by the courts and the ICC. See, e.g., *Green Bay & Western Railroad* v. *United States of America* (Ann Arbor case), 644 F.2d 1217 (7th Cir. 1981); *Cancellation of Intermediate Routing—Michigan Northern Railway*, 361 ICC 224 (1979).

EX PARTE NO. 389

Section 217 of the Staggers Act established certain cost and revenue guidelines, and also required the ICC to promulgate appropriate rules and regulations for the implementation of the new section. Pursuant thereto, the Commission published interim rules and received comments thereon in a proceeding entitled Ex Parte No. 389, Procedures for Requesting Rail Variable Cost and Revenue Determinations for Joint Rates Subject to Surcharge or Cancellation.

The presently applicable procedures, published at 46 Fed. Reg. 19238, 3/30/81, compound the confusion and error inherent in Section 217 of the Act.

For example, the basic cost data used by the Commission in making revenue to variable cost determinations is the 1977 Rail Form A. While this data is "updated" through the use of a multiplier factor, the plain fact is that the data is four years old. Thus, in the case of ConRail, there is no adjustment for the very substantial cost reductions and operating changes which have taken place due to recent management actions.

Likewise, even though the State of New York has invested many millions of dollars in ConRail's routes and facilities within the State, and has given substantial tax relief, none of this taxpayer contribution is reflected in the cost figures which are used. In other words, when computing the cost of a movement via ConRail to or from Long Island, the taxpayers here are not getting any credit for their substantial reduction of ConRail's costs.

Another difficulty is the route mileage used in computing variable costs. In the case of the LIRR, for example, southern traffic must be routed via Selkirk, New York—almost 150 miles north of New York City. As a direct result of the so-called "Selkirk Hurdle", cost via this route are substantially higher under the ICC formula than to points in nearby New Jersey or New York, west of the Hudson River. What is *not* taken into account is that the "Selkirk Hurdle" is of ConRail's making; in the past this circuit could have been avoided by use of the car floats across New York Harbor or the Poughkeepsie Bridge route. These routes were eliminated for ConRail's convenience, and now the shippers and receivers are being asked to pay for the extra cost of operating through the "Selkirk Hurdle".

Another problem with the Ex Parte 389 procedure is the unconscionable burden placed on shippers and receivers. The surcharging or cancelling carrier has no obligation to establish that movements fail to meet the 110% revenue-to-variable-cost test; this burden is entirely on the shipper or receiver. In many cases the

[1] App. B has been retained in committee files.

revenue or cost varies substantially with routing and the skipper has no way to find out which route will bear the lowest surcharge. The only way to "test" the surcharge is on a trial and error basis, shipping cars along all possible routes and then performing the required mathematical analysis.

In short, Section 217, when coupled with the ICC's procedural rules in X–389, creates a traffic manager's nightmare and an unconscionable administrative burden on the shipping public.

SURCHARGES—PULPBOARD, PAPER, ETC.

In February 1981, ConRail announced its intention to impose surcharges on certain commodities moving from the south to the northeast, including pulpboard, wrapping paper, wallboard, insulating material, malt liquors, brick, etc. Initially, ConRail proposed "blanket" surcharges to be uniformly applied to all points within the territory. Typical surcharges range from $250 per car (wrapping paper) to $440 per car (insulating material). One outcome of the Commission's finding in Ex Parte No. 389 was essentially that the revenue-to-variable-cost test must be applied to the specific route for each movement. Using the procedures established by the Commission, numerous shippers and receivers applied for—and obtained—substantial reductions or cancellations of the surcharges applicable to their shipments. Other shippers and receivers applied for reductions of the surcharge, but received little or no relief. The reductions and cancellations were published by ConRail as exceptions to the uniform per-car surcharges in the various tariffs (See CR Tariff No. 9528–A).

It soon became apparent, when the exception tariffs were published, that rate parity within the New York rate group has been completely upset by the unequal application of the surcharges. A clear pattern was visible—especially with regard to receivers located on Long Island. In almost every case, Long Island receivers of pulpboard, paper and similar commodities were paying the full surcharge, while their competitors in nearby New Jersey or southern New York State were paying no surcharge.

The economic impact of this rate discrimination is huge. Pulpboard and wrapping paper account for about 6000 car loads per year—about 15% of the total tonnage carried by the LIRR. At $250 per car, Long Island manufacturers of corrugated boxes, paper bags and similar products will be paying $1.5 million more per year in frieght charges than their nearby competitors. Impacts of the same order can be estimated for receivers of building materials, insulation and other surcharged commodities.

Due to the fact that these are "captive" users and that freight costs are such a significant part of their total manufacturing cost, most of these companies will not be able to compete against their rivals who are exempt from the ConRail surcharges.

JOINT RATE CANCELLATIONS—GRAIN, ETC.

In another unilateral rate action, which was protested by shippers, receivers and other railroads, ConRail cancelled joint rates on grain, grain products and other important commodities. In place of the joint rates, ConRail instituted its own "local" rates which apply to all movements from, to or via its lines. The principal commodities affected are bulk and bagged flour used by bakeries, manufacturers of spaghetti, noodles and similar products. Whole grains used for animal feed are also affected.

The new ConRail rates are "incentive rates", i.e., the rate is lower for larger, more heavily loaded rail cars. In a few cases, for shippers or receivers on a ConRail siding, the rates are lower than those previously in effect. However, for most customers, especially those served by one of ConRail's connecting railroads, there will be a significant increase in freight charges.

For example, a receiver in Brooklyn or Queens served by the LIRR, on a 100,000 lb. shipment of flour from Buffalo, formerly paid $1.51 per cwt and now will pay $1.88 per cwt—an increase of $370 per car. On a typical 150,000 lb. movement from the midwest, the increase would be about $630 per car. Receivers served by New York Dock/Brooklyn Eastern District Terminal will have similar increases in their freight costs.

Because of the ConRail rate action and the fact that its connecting lines such as the LIRR or the NY Dock/BEDT have to cover their costs too, rates to destinations on these railroads are now much higher than to nearby points served directly by ConRail.

For example, on the 100,000 lb. flour shipment from Buffalo discussed above, a ConRail customer in Oak Point (Bronx), Jersey City (New Jersey) or Bay Ridge

(Brooklyn) would only pay $1.39 per cwt. His neighbor served by BEDT would pay $1.71 per cwt (plus about 25 cents per cwt local trucking charge) and a LIRR customer would pay $1.88 per cwt. Obviously, the result of ConRail's action is to discriminate against other railroads such as the LIRR and NY Dock/BEDT and their customers.

Once again, this action by ConRail has completely disrupted the rail rate structure in the New York area and destroys the rate parity which has existed for almost a hundred years. Many rail users in Brooklyn, Queens, Nassau and Suffolk will be badly hurt and will not be able to compete in this market area with competitors from New Jersey.

The impact on ConRail's connecting carriers is also very serious, see Docket No. 38689, Restructured Rates on Grain & Grain Products, ConRail. The New York Dock and Brooklyn Eastern District Terminal Railroads, in particular, stand to lose almost 50 percent of their traffic. If they went out of business, it would hurt not only the flour receivers, but everyone else they serve.

LEGISLATIVE OVERSIGHT

While it is evident that Congress, in passing the Staggers Act, was aware of ConRail's need for immediate revenue relief, it is doubtful and many legislators could have anticipated that traditional rate structures would be destroyed and that particular region like Long Island would be the victim of destructive rate practices. Few, if any, anticipated that rate parity would be upset within the New York rate group, with such extreme prejudice to Long Island's rail users and to the smaller connecting carriers. The term "legislative oversight" is well suited to describe the regional imbalance which has been caused by Section 217 of the Staggers Act.

RECOMMENDED CORRECTIVE ACTION

If unilateral surcharges are to be allowed at all, it is clear that corrective legislation is mandated to preserve the traditional rate parity within commercially competing regions. See, for example, the language incuded by Congress in the Railroad Retirement Act amendments of 1973, which authorized the railroads to recoup increased taxes through rate adjustments. P.L. 93-69, Title II, Section 201, 87 Stat. 166, 1973, adding new section 49 U.S.C. 15a(4)(e):

"Any increased freight rates authorized shall not exceed a reasonable level by types of traffic, commodities, or commodity groups and *shall preserve existing market patterns and relationship and present port relationships* by increased limitations within and between the major districts to the extent possible without authorizing unreasonable increases in any district." (emphasis added)

Even if such corrective legislation requires averaging of revenues and costs within the rate group and some cross-subsidization among the traffic, it must be done to prevent severe economic and social dislocation.

It should not be overlooked that unilateral surcharges are a very undesirable way of correcting what is essentially an underlying divisions problem. ConRail's revenue short fall can be traced in most every case to an inadequate share (or division) of the joint freight charges, with southern and western carriers receiving revenue disproportionate to their costs.

Section 218 of the Staggers Act is entitled, "Expedited Division of Revenues Proceedings" and it, together with prior 4R Act legislation, is intended to help rail carriers solve their divisions problems within specified short time limits. 49 U.S.C. 10705.

Unfortunately, ConRail has chosen to ignore its remedies under this section, leaving all of the underlying divisions inequities unsolved.

Surcharges and joint rate cancellations create havoc as far as rate parity is concerned. They also create procedural and tariff nightmares for shippers, receivers and for the railroads.

The obvious answer would be to repeal the section authorizing surcharges and joint rate cancellations, and force the carriers and the ICC to straighten out the basic divisions problem, utilizing the procedures set out in Section 10705 of the Interstate Commerce Act.

WHAT IF NOTHING IS DONE?

There are about 200 companies on Long Island, according to FUA estimates, which will suffer from the impact of ConRail surcharges and joint rate cancellations.

Depending on the degree of specialization of their products, their market areas and profit margins, some will go out of business, some will relocate off Long Island,

and some will stay put and tighten their belts for as long as possible. For the most part, trucking is not a viable alternative; even low cost contract carriers, agricultural cooperatives, independents seeking backhaul traffic and other "bargains" are unable to compete with rail and are generally unreliable. Perhaps barges may be a partial answer for bulk shipments from certain origins, but this would require double handling in most cases.

The problem is that many commodities almost universally move by rail. Shippers and receivers have built their mills and plants near rail lines and have invested heavily in rail sidings and facilities. Not just the companies, but their employees and the communities, have located and structured their operations based on a stable rail system—one essential part of which is rate parity within a territory or regional market area. Unless immediate legislative action is taken, serious economic and social consequences will result.

APPENDIX

Regular: J. & L. Adikes, Inc.; Agway Inc., Fertilizer Divn.; Ajayem Lumber Corp.; AMCO Plastic Materials, Inc.; American Lumber Co., Inc.; Joseph Aronauer, Inc.; Baisley Lumber Corp.; Beacon Milling Co.; Blade & Holzhauser, Inc.; Bleyer, Alfred & Co.; Boening Bros., Inc.; Boro Lumber Co., Inc.; Canover Industries, Inc.; Certified Industries, Inc.; Combined Container Industries; Esselte Pendaflex Corp.; Feldman Wood Products Co.; M. Fine Lumber Co., Inc.; Fink Baking Corporation; Fruitcrest Corp.; Gallo Wine Distributors, Inc.; Georgia Pacific Corp.; Global Sysco Corp.; Greenman Bros.; Guinness-Harp Corporation; H–G Toys, Inc.; House of Fodera; Independent Chemical Corp.; International Salt Company; Kleet Lumber Co., Inc.; Lin Pac Corrugated Container Corp.; Lorraine Textile; Lynmar Lumber Industries; Macrose Industries Corp.; Manufacturers Corrugated Box Co.; Mid-Island Lumber & Supply; Nash Lumber Merchandising Corp.; N.Y. Association for the Blind; Phelps Dodge Corporation; Philipp Brothers Divn. Engelhard; Quintree Distributors; Reserve Supply Corp.; Riverhead Building Supply; Ronzoni Foods, Inc.; Ronzoni Macaroni Co., Inc.; S & K Farms, Inc.; Herbert H. Sabbeth Corp.; St. Regis Paper Company; Samson Paper Bag Co., Inc.; Santini Bros., Inc.; G. Schwartz Lumber Co., Inc.; Simkins Industries, Inc.; Smith Chemical & Color Co.; Southern Container Corp.; Star Corrugated Box Co.; Suffolk Agway; Thypin Steel Co., Inc.; H. Verby Company, Inc.; Waldbaum, Inc.; White Pine Sash; White Rose Food Corp.; Wiener and Waters, Inc.; and Woodex Lumber Corp.

Associate: Anco Wood Spec. Inc.; Atlas Traffic Consultants; Freight Services Improvement Conference; Harmon Paper Stock Co., Inc.; Ideal Toy Co.; Larkfied Lumber; L.I. Wholesalers; Mars Cup Co., Inc.; Muran Wood Products; D.J. Mytelka & Associates; Packard Flooring Supply Co.; Plywood Distributors, Inc.; Professional Air Cargo, Inc.; Southampton Lumber; and Steinway & Sons.

STATEMENT OF THE PUBLIC UTILITIES COMMISSION, CITY OF HIBBING, MINN.

The Public Utilities Commission of the City of Hibbing, Minnesota, submits the following statement on the effect of the Staggers Rail Act for inclusion in the record of the Subcommittee's oversight hearing of November 10, 1981. We appreciate this opportunity to inform the Subcommittee of our experience with the Act.

The Hibbing Public Utilities' single steam generating plant is located in the City of Hibbing, County of St. Louis, State of Minnesota. The plant is a co-generation plant serving some 8,000 electric customers and 1,500 steam heat users directly from a district hearing system. The plant's three steam boilers are coal-fired, burning sub-bituminous "C" coal shipped by rail from Colstrip, Montana, Via Burlington Northern trackage. The railroad in question handles 100 percent of the fuel requirements of the Hibbing Plant in its entirety from the mine to our track hopper.

The Hibbing Public Utilities Commission is in a position where absolute dependence for transportation of our fuel is in the hands of a single carrier, and our position is that, without some degree of restraint on freight rates, the railroad could raise rates to an unreasonable level not consistent with the public interest.

It has been our understanding that the intent and purpose of the market dominance concept was to maintain commission rate jurisdiction where te market itself is not sufficiently competitive to insure just and reasonsble freight rates. One approach could be based on the cost of service to a shipper in those areas such as Hibbing, Minnesota, where there is sufficient reason to believe that the condition of market dominance is in existence.

This is clearly the case of the Hibbing Public Utilities Commission, as there is no other rail carrier to shift to in coal movement. As our coal is contracted with mines

in Western Montana, the transportation of coal by motor carrier is economically unrealistic.

Further, our plant is basically coal-fired, but two boilers are fitted to burn natural gas, but the economics of gas consumption and the gas curtailment schedule as ordered by the Federal Energy Regulatory Commission at Step 7 would not provide us with adequate fuel supplies of this nature on a fully dependable basis. Therefore, there is no alternative to our current situation, as we cannot take advantage of the contract rate provisions of the Staggers Act as a viable approach to cost control, as the complete lack of competition for rail traffic into our area would not provide us with a basic bargaining position. Further, it is doubtful if the rail carrier would enter into such contract discussions as a willing party.

Recently, we found it necessary to approach the Burlington Northern Railroad on the subject of equalization of rates on traffic from the Montana Fields between two mines situated in the same locale that would have been beneficial to this Utility by contracting for lower cost fuel of the same characteristics, but that request did not reach a successful conclusion. This was due to the Burlington Northern insistence that the 25¢/Ton disparity in rates from the same coal field was justified as far as they were concerned. However, this utility still takes the position that the rate disparity was not totally justified.

It appears to us that, if some degree of restraint is not exercised to control rate increases, carriers will take advantage of their particular position to levy increases all out of porportion to that necessary to maintain a reasonable return on investment in railroad and directly related facilities.

Coal movement, by far, exceeds any other commodity moved by rail and is increasing at a steady rate. Complete freedom to establish rates that could prove excessive on this coal movement would not be in keeping of the policy to "encourage and promote the energy independence at rates which do not exceed a reasonable maximum where there is an absence of the effective competition." [1]

It is therefore, the feeling that this Utility would suffer adverse effects due to the absence of both rail competition and plentiful comparable cost competition fuels in our area of service.

Excessive rail rates would have a serious impact on our power rate structure resulting in higher costs to our consumers.

We would like to point out that, being a cogeneration plant, a vast majority of our district heating system customers are the elderly housed in single residential homes and in apartments. The unwarranted increase in freight rates would doubly adversely affect this group of our citizenry by both increased power bills coupled with an increased heating cost. In a geographical location where winter temperatures of −40°F are not uncommon, the effect on the consumer during these inflationary times would be devastating.

We, therefore, urge the Subcommittee to consider carefully the market dominance question and the possibility of new legislation to make sure that market dominance is restored as a fair standard for determining where rate regulation is necessary. In addition, we believe it may become necessary for the Subcommittee to recommend legislation which would require the ICC to place some degree of restraint on movement rates by rail that are cost-justified and fair to all parties concerned. It appears to us that the public interest needs some degree of protection.

Statement of the United Fresh Fruit and Vegetable Association

My name is Bernard Imming. I am President of the United Fresh Fruit and Vegetable Association, headquartered in Alexandria, Virginia. Submitting testimony with me is Patrick Boyle, United's Transportation Counsel. I wish to commend the Surface Transportation Subcommittee of the Committee on Commerce, Science and Transportation for conducting this oversight hearing. In addition, I wish to thank the Committee and its Chairman for permitting United this opportunity to submit its comments on the implementation of the Staggers Rail Act of 1980.

United is the national trade association representing the fresh fruit and vegetable industry. Its membership numbers over 2700 companies located in nearly all of the states. They are engaged in all facets of the fresh produce industry and include growers, shippers, receivers, wholesalers, retailers, produce and truck brokers, as well as motor, air, water and rail carriers. Collectively, the members of United handle more than eighty (80) percent of the fresh fruits and vegetables which are

[1] The Conference Report, Staggers Act, Rail Transportation Policy.

commercially marketed in the United States; a thirty-five (35) billion dollar a year industry.

A number of the provisions of the Staggers Rail Act affect the rail transportation of fresh fruits and vegetables, and United will gladly respond to the Subcommittee's request for information on any one of them. For the purpose of this oversight hearing, however, United will limit its testimony to two sections of the law: first, Section 211 entitled "Permissive Limited Liability Rates" and Section 213 captioned "Exemption." Both of these sections of the act affect the cargo liability standards for the rail movements of all commodities, regulated and exempt.

BACKGROUND

Rail liability standards for loss of and damage to cargo, such as fresh fruits and vegetables, are based on the traditional principals of bailment developed at common law. Under this longstanding principle a rail common carrier assumes absolute liability, with few exceptions, for any loss of or damage to the cargo which it transports.[1] In 1906, Congress adopted the Carmack Amendment to the Interstate Commerce Act, which embodies this general rule of common law.

The Carmack Amendment neither creates new substantive rights for shippers nor imposes any new obligations on the railroads beyond those developed at common law. Instead, the amendment merely sets forth convenient and well-recognized procedures for shippers and carriers to follow in settling loss and damage claims.

Although part of the Interstate Commerce Act, the Carmack Amendment was neither intended to be nor has ever become part of the transportation regulatory scheme. Consequently, in 1979 when the Interstate Commerce Commission exercised its authority to exempt the rail transportation of fresh fruits and vegetables from the regulatory provisions of the Interstate Commerce Act, shippers and receivers of fresh produce logically and reasonably assumed that the common law principles of absolute liability would remain in effect.[2]

Pursuant to this decision of the Commission, a number of rail carriers begin to interpret the exemption order as also freeing them from traditional common carrier responsibility for loss of and damage to fresh fruits and vegetables. As a result of this unfounded interpretation, basic common law liability standards, incorporated in the Carmack Amendment, were being unilaterally negated by some railroads through terms and conditions of "exempt" bills of lading offered to shippers and receivers of the exempted perishable commodities on a "take it or leave it" basis. Under these contracts the ability of a shipper to recover for loss of and damage to its cargo, while in the sole possession of the rail carrier, is greatly reduced and, as a practical matter, frequently eliminated.

Similar confusion arose concerning the applicability of Carmack Amendment liability standards on the rail movement of exempt commodities when the Interstate Commerce Commission exercised its authority under Section 213 of the rail act, codified at 49 U.S.C. 10505(f), "to exempt transportation that is provided by a rail carrier as part of a continuous intermodal movement." Accordingly, in Ex Parte No. 230 (Sub. No. 5), Improvement of TOFC/COFC Regulation, 46 Fed. Reg. 14348 (1981) codified at 49 C.F.R. 1039, 1090 and 1300, the Commission exempted "rail and truck service provided by rail carriers in connection with trailer on flat car (TOFC) and container on flat car (COFC) service from economic regulation." A number of shippers and receivers were concerned that the exemption order might be interpreted by the railroads as relieving them from the provisions of the Carmack Amendment concerning their liability for loss and damage. In response to a petition for declaratory order, the Commission clarified this question stating that "railroad tariffs or contractual items on TOFC/COFC service which violate the terms and conditions of the Carmack Amendments are unenforceable as a matter of law." See 46 Fed. Reg. 32257 (1981).

[1] Pursuant to interpretations by the Supreme Court, a rail common carrier is liable for the full actual value of loss of or damage to goods transported by it unless it can show that the loss or damage is attributable to an act of God, the public enemy, the act of the shipper himself, public authority or the inherent vice of the nature of the goods. See, *Missouri Pacific R. Co.* v. *Elmore & Stahl*, 377 U.S. 134 (1964), rehearing denied, 377 U.S. 948.

[2] The exemption authority of the Commission is contained in Section 10505 of the Interstate Commerce Act, 49 (U.S.C. § 10505.) *See*, Ex Pare No. 346 (Sub. No. 1), *Rail General Exemption Authority-Fresh Fruits and Vegetables*, 44 Fed. Reg. 18227 (1979) Codified at 49 U.S.C. § 10526(a)(6)(E).

THE STAGGERS RAIL ACT OF 1980

In an attempt to prohibit a railroad from contracting away its responsibility for cargo liability, the Staggers Rail Act of 1980 reaffirms the applicability of the Carmack Amendment liability standard to rail movements of exempt commodities, such as fresh fruit and vegetables. Specifically, Congress included Section 213 in the act, codified at 49 U.S.C. 10505(e), which states that "no exemption order . . . shall operate to relieve any rail carrier from an obligation to provide contractual terms for liability and claims which are consistent with the provisions of Section 11701 [The Carmack Amendment]. . . ."

In addition, Section 211 of the Staggers Rail Act directed the ICC and the Department of Justice to study independently the continuing need for Carmack Amendment liability protection and to submit its legislation recommendations to Congress by October 1, 1981. By notice published in the *Federal Register* issue of March 20, 1981, 46 Fed. Reg. 17893 (1981), the Commission solicited written comments from interested parties for its study. On behalf of an industrywide coalition, United submitted comments and a reply statement to the Commission in June and July of 1981, respectively. After reviewing the numerous comments which it received, the ICC submitted its final report to Congress on September 29, 1981.

In Ex Parte No. 403, Cargo Liability Study; Report to Congress, Id., the Commission concludes that the Interstate Commerce Act should be amended to eliminate the venue restrictions contained in the Staggers Rail Act of 1980 because they appear to be unduly severe. Also, the Commission recommends an amendment to the act to remove the $10,000 jurisdictional threshold for access to the Federal Courts and to treat litigation arising under the Carmack Amendment as a federal question, regardless of the dollar amount of the claim involved. According to the report, a further recommended amendment to the Interstate Commerce Act would provide the courts with the authority to award attorneys fees to successful claimants absent an equitable, efficient and inexpensive arbitration program.

Moreover, in the report the regulatory agency states that it does not support the adoption of a comparative negligent standard in cargo liability cases or the implementation of a no-fault liability concept. In addition, the Commission does not recommend to Congress a change in the present burden of proof developed at common law which a shipper or receiver must meet to establish its loss and damage claim. The views of the Commission expressed in this report, which this subcommittee has received, are consistent with the position of United and its members.

Of particular interest to shippers and receivers of fresh fruits and vegetables is the concluding statement in the Commission's report that the agency will continue to require rail carriers to offer rates for full liability protection. On the other hand, the agency does note that it lacks jurisdiction over the reasonableness of the full value rates offered by the railroad in situations where the shipper or receiver has available to it alternate modes of transportation. Accordingly, the Commission indicates to Congress that the practical effect of this jurisdictional restriction on its authority is to provide shippers and receivers with a right to be offered rates for full liability protection, but without an administrative remedy to challenge unreasonable or excessive rates. Because members of the fresh fruit and vegetable industry have been offered by the railroads "unreasonable or excessive rates" for full liability protection without administrative recourse, United felt compelled to testify before this subcommittee on the matter.

IMPACT UPON THE FRESH FRUIT AND VEGETABLE INDUSTRY

As discussed, supra, the Carmack Amendment to the Interstate Commerce Act embodies long-standing principles of rail common carrier liability developed at common law. This absolute liability standard was applicable to rail transportation prior to the creation of the Interstate Commerce Commission and it was specifically incorporated in the Interstate Commerce Act by Congress in 1906. In the Staggers Rail Act of 1980, Congress reaffirmed the applicability of the liability standard for loss and damage claims and specifically stated in Section 213 of the act that it even applies to the rail transportation of exempt commodities, such as fresh fruits and vegetables, and exempt service, such as rail TOFC/COFC movement. More recently, as noted above, the Interstate Commerce Commission has solicited and received public comments concerning the continued viability of Carmack Amendment liability standards. The record developed in Ex Parte No. 403, supra, provides ample justification for maintaining the current standards and procedures for loss and damage claims. Accordingly, the Commission has conveyed to Congress and to this subcommittee in its Cargo Liability Study; Report to Congress, containing the sup-

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government control over the country's beleaguered railroads. Two of the major providions of the bill that the short line carriers were extremely concerned with were the surcharge and the joint rate provisions. While these can serve to be a useful tool for the larger railroads to eliminate non-profitable traffic, the method required in the Staggers Act to permit a protest leaves much to be desired; that the burden of proving that the assailed rate is in excess of that permitted is on the shipper and/or small carrier, viz., the Class III carrier.

The Staggers Act does provide some relief for the small carriers in that they may secure some help from the Interstate Commerce Commission. However, prior to the Commission performing this service, the small carrier must expend a great deal of time and effort in the preparation of documentation for the Commission to work from. Most small carriers do not have the manpower nor the expertise to carry this out within the allotted time frame.

It is understood and we greatly appreciate Congress permitting a review of these provisions after a one-year period. This period is coming to a close and a decision must be reached in the immediate future. We recommend that these provisions be subject to a yearly review by Congress. One of our primary reasons for making this request is our feeling that in the start-up year Conrail has been busy with; many of their larger movements and they have had insufficient time to address the smaller movements that will affect the Class carriers. However, as time goes on, we believe that we will see a rash of additional surcharges applied to the detriment of the small carriers.

The mergers that are taking place within the United States will continue to create extremely large rail systems. It will become more and more difficult for the small carrier in the rural areas to have much of a voice.

Conrail has notified the Commission and others of their intent to abandon large segments of their system. Unless numerous small carriers are able to create a viable operation on these abandoned lines, many of the cities and towns affected will be left without any rail service at all.

This letter, while it does name Conrail in great detail, is not to criticize the management of Conrail for their efforts to make their line viable. To date, the Vermont Railway has only experienced these difficulties with Conrail.

We on the Vermont Railway have had experience with a surcharge on our major outbound commodity, limestone. We have utilized the cost revenue analysis service of the Interstate Commerce Commission and we are still working with Conrail in an effort to resolve our differences. We have not filed a formal protest with the Interstate Commerce Commission. However, we do believe that we were remiss in not joining other carriers in the protest of Conrail's elimination of joint rates on grain and recyclables. Our major problem was that we were inundated and we did not have ample time with our available manpower to prepare the necessary documentation. This is one of our great concerns for the future as this can occur at any time.

It is our belief that the surcharging or cancelling carrier should prove upon submission, to the Commission, that he is not receiving the revenue-to-cost ratio described in the Act.

We fully appreciate your consideration of our feelings on this issue. If we may furnish additional information, please contact us.

Very truly yours,

JOHN R. PENNINGTON,
President.

SCHWARTZ METALS GROUP,
Des Moines, Iowa, November 6, 1981.

Hon. JOHN C. DANFORTH,
Chairman, Subcommittee on Surface Transportation, Committee on Commerce and Transportation, Dirksen Office Building, Washington, D.C.

DEAR CHAIRMAN DANFORTH: Schwartz Metals is an Iowa-based company with operations in Des Moines, Marshalltown, Ottumwa and Cedar Rapids, Iowa, Tulsa, Oklahoma, and Denver, Colorado. Schwartz Metals is involved in various phases of the metals business, one of which is the collection and processing of scrap metal, both ferrous and non-ferrous. As scrap re-cyclers of our nation's precious resources, our primary mode of transportation to the mills and foundries has been the railroad. This relationship with the railroad has had its ups and downs over the past decades. However, the past year our problems, transportation costs and equipment availability, have gotten out of control. The cost of transporting by rail has skyrock-

eted in the last year while the availability of gondola cars, necessary for the shipment of scrap metal, has never been worse.

Transportation costs are an important concern in the overall competitive situation of our domestic industries. The following rate increases is an indication of the rising transportation costs:

	Percent	Amount
Oct. 15, 1979 (Ex Parte 368)	15.5	$1.555
Dec. 31, 1980 (Ex Parte 386)	5.0	1.213
May 11, 1981 (Ex Parte 375C)	20.9	1.466
Oct. 1, 1981 (RCCR X003)	8.4	1.589
Accumulated increase	49.8	

Further complicating this situation is the fact that scrap prices will probably hit a ten-year low during the last quarter of 1981.

Not only have transportation costs increased 49.8% over this period, but the availability of gondola cars is a never-ending problem. The size of the overall gondola fleets has steadily declined from 294,202 in 1954 to 163,694 in January, 1978. The most recent figures shows 145,275 in service as of August 1, 1981. The pool of gondolas available to scrap processors is further restricted by the fact that a substantial number of gondolas are "equipped", specially designed to carry certain products to the exclusion of scrap.

Over the past 100 years, railroads have had to operate through and under a maze of federal and state rules and regulations. As scrap processors, we recognize the importance of maintaining railroad profitability, and therefore, to pay an appropriate share of freight increases. However, we do not believe there is room for rate increases such as those taken in the past 2 years. Schwartz Metals would prefer to continue to transport its scrap metal by rail. But poor service, the unavailability of gondola cars and tremendous price increases in the last two years have forced us to turn to alternate modes of transportation, incuding common carrier and private truck fleet. The attached chart shows the comparative costs of shipping scrap ferrous materials by rail, common carrier and by private fleet. The savings involved in shipping by private fleet or common carrier are obvious.

It now has been over one year since President Carter signed the Staggers Rail Act of 1980. This legislation has presented opportunities to the rail industry. The most important opportunity is that the railroads now have the freedom to contract equipment, rates and service to meet specific customer needs.

The aims of the act are laudable. It remains to be seen whether the goal of the Staggers Act, a healthy, viable, rail system, can or will be accomplished. It is hoped that the imagination and creativity of the railroad comes to the forefront soon.

Sincerely,

JOSEPH L. KENNEALLY,
Traffic Manager.

Attachment.

TO:	Wilton, IA	Keokuk, IA	Chicago, IL	Peoria IL	Sterling IL	Kansas City	Pueblo CO	Norfolk NB
Des Moines	159	176	326	253	229	195	730	224
Rail	19.37GT	18.62GT	25.54GT	22.30GT	22.30GT	19.27GT	40.07GT	22.96GT
Common Carrier	14.50GT	16.20GT	27.07GT	18.89GT	16.70GT	15.45GT	51.38GT	16.70GT
Private Fleet	7.10GT	7.85GT	14.50GT	11.25GT	10.65GT	8.65GT	32.45GT	10.00GT
Marshalltown	134	182	289	234	192	245	780	246
Rail	18.62GT	18.62GT	22.96GT	22.30GT	19.37GT	22.96GT	41.54GT	22.96GT
Common Carrier	12.80GT	17.10GT	22.38GT	17.64GT	15.45GT	18.89GT	54.92GT	18.89GT
Private Fleet	5.95GT	8.10GT	12.85GT	10.40GT	8.55GT	10.90GT	34.65GT	10.95GT
Cedar Rapids	72	120	221	168	124	311	848	310
Rail	15.55GT	18.62GT	22.32GT	18.63GT	16.38GT	22.98GT	46.10GT	27.00GT
Common Carrier	8.00GT	11.10GT	16.70GT	12.84GT	9.69GT	24.37GT	60.28GT	24.37GT
Private Fleet	3.25GT	5.35GT	9.85GT	7.50GT	5.50GT	13.80GT	37.64GT	13.80GT
Ottumwa	107	90	286	169	189	216	790	309
Rail	16.38GT	15.54GT	22.96GT	18.62GT	19.37GT	19.37GT	41.55GT	25.53GT
Common Carrier	10.20GT	9.40GT	22.38GT	12.84GT	14.46GT	16.55GT	55.31GT	24.37GT
Private Fleet	4.75GT	4.00GT	12.70GT	7.50GT	8.40GT	9.60GT	35.06GT	13.70GT

Rail = Single Car Movement

Common Carrier = Single Truck Load - Does not include Fuel Surcharge of 18%

Private Fleet = Single Truck Load costs to move load one way

THE WRIGHT-LORENZ GRAIN CO., INC.,
Salina, Kans., November 13, 1981.

Mr. MIKE PETTIT,
Senator Bob Dole Office, Dirksen Building,
Washington, D.C.

DEAR MR. PETTIT: In reply to your inquiry regarding problems the grain industry has had with the implementation of the Staggers Act, I submit the following:

There are some questions that need to be raised and clarified:

1. Are railroads as common carriers a public utility?
2. Are railroads pescribed by law to provide service to *all* the public equally?
3. Can railroads pick and choose what and for whom they will haul?

The Elkins Act states "It shall be unlawful for any person, persons or corporation to offer, grant or give or to solicit, accept or receive any rebate, concession, or discrimination in respect to the transportation on any property in interstate or foreign commerce by any common carrier."

The cash grain markets are in a complete state of confusion because we do not know from day to day what the freight rates will be to any destination from any origin or even if you will be able to get thru rates or equipment on multiline shipments. We cannot give a farmer a firm price for his grain for future shipment as we do not know if there will even be a rate or route. We have had situations in multiple rail towns where one railroad refuses to switch the empty equipment of a competing railroad to an elevator on its siding. Most all elevators are located on one railroad siding and the town may be served by as many as four railroads as is Salina, Kansas. It may be impossible to take advantage of the best competitive rate because one railroad refusal to switch competing railroad equipment.

Since the Staggers Act we also have certain railroads forcing the purchase of rail sidings by elevators that have been built on railroad leases. For the past 100 years, railroads have built sidings to attract business and leased part of these sidings to elevators to build in order to be able to ship on the railroad. Now some of these railroads are threatening to cancel the leases and pull up the siding if the elevator did not buy the siding which the railroad built several decades ago. They also threatened that if the elevator did not buy the siding that they would "reevaluate" the lease. We have concrete elevators that were built 40 to 50 years ago located on siding built 100 years ago where this is happening. This is the attitude of some railroads since the deregulation act was passed.

The way the Staggers Act "Captive Shipper" test is written, it would make it impossible to prove by the shipper. This portion of the act was patterned after the Canadian requirements and no one has been able to meet the requirements even in such a sparcely settled country as Canada. These requirements should be liberalized in favor of the "Captive Shipper".

Under the present Staggers Act, there is a concentration of cheap rates in the hands of a few. The multinational grain companies such as the Continentals, Cargills, Bunge, Dreyfus, etc have the clout to negotiate cheap rates as the heads of those companies are socially personal friends of the railroad chief executives and are able to secure an unfair advantage over the smaller firms. It is known that whoever sets the rates for rail transportation of grain and controls the availability of rail service ultimately controls who owns the grain and its value. We feel the smaller firms are being made to subsidize the large firms cheap rates thru their higher rates.

I quote from a 1979 D.O.T. analytical paper that describes the rail industry as being in a state of crisis "the railroad system as a whole is being forced to provide service at revenue levels that do not cover the full costs." This was in 1979 when the railroads were asking for monthly increases in rates. I am listing four Kansas towns with the effective grain rates per cwt on June 6, 1979 and on October 1, 1981 to Kansas City and to the gulf.

[Amounts in cents]

	KC 1979	KC 1981	Percent change	Gulf 1979	Gulf 1981	Percent decrease
Salina	59½	47	−21	108	80	−26
Colby	84	90	+3	138½	133	−5
Ellis	68½	71	+7	117	111	−4

	KC 1979	KC 1981	Percent change	Gulf 1979	Gulf 1981	Percent decrease
Wellington	59⅛	63	+6	94	80	−15

This shows that in the past 28 month period, there has been an average increase of 5 percent in 3 rates while 5 rates have decreased an average of 14 percent. The railroads were giving figures during the Staggers hearings, showing the need for more money in 1979. Now with the reduction in rates it makes you question the accuracy of the 1979 figures the railroads furnished.

As I have stated on many occasions, we want the railroads to make money and be free of government regulations only to the extent that all shippers are treated equally. The railroads lines that are here now are all we will have, they can not be moved and no new lines will be built. The railroads will want to abandon as many of the small lines as possible so our total rail milage will from now on, be on the decline. The railroads are monopolistic as they can not be moved and no more will be built. I therefore feel some control, as any public utility, should be imposed to eliminate discrimination of rates and equipment. We feel some rail executives have taken this power of deregulation of a monopolistic situation and used it unfairly.

Very truly yours,

KENNETH L. WRIGHT.

EVANS GRAIN CO.,
Salina, Kans., November 18, 1981.

Senator ROBERT J. DOLE,
Dirksen Senate Office Building,
Washington, D.C.

Senator NANCY LANDON KASSEBAUM,
Russell Office Building,
Washington, D.C.

DEAR SENATORS DOLE AND KASSEBAUM: We understand that the Surface Transportation Sub-Committee of the Senate Commerce, Science and Transportation Committee is in the process of conducting oversight hearings on the Staggers Rail Act of 1980.

We have previously expressed our concern and our opposition to the contract rate provisions which are included in Section 208 of the Staggers Rail Act of 1980 (49 USC 10713). The use of contract rates in connection with the sale of wheat and feed grains has created complex marketing problems, disrupted the futures markets for these commodities and has operated to the distinct disadvantage of the small shippers.

The price of wheat and feed grains at the local country elevator is determined by reference to the current option price on the futures market adjusted for freight from the country elevator to the designated futures market. When the cost of freight from the country elevator to the designated market is uncertain, the uncertainty is reflected in the price which the country elevator can offer for the commodity. Historically freight costs have been a neutral factor in competition between country elevators and other grain purchasers and merchandisers. With the contract rate provisions in effect, the country elevator, grain purchaser or merchandiser who can negotiate the lowest freight rate has a distinct advantage over any competitor.

It seems unnecessary to state that a shipper would not enter into a contract for the shipment of agricultural commodities unless the contract rate was less than the common carrier rate that would otherwise be applicable to the shipment of those commodities. Except under unusual circumstances, a contract rate would almost always be for a rate which would be less than the single car shipper could utilize under the tariffs applicable to common carrier shipments. Since the marketing of these agricultural products is highly competitive and price differentials of a fraction of a cent per bushel determine the market, it is apparent that the country elevator that is shipping these commodities on the common carrier tariff rates will be unable to compete with the country elevator who has the benefit of a contract rate. Within a relatively short period of time the elevator that must rely on the common carrier rate is either going to be out of business or owned by the elevator with the favorable contract rates.

It is clear that the rail carrier would not be anxious to enter into contract rates with a shipper unless there are substantial volumes committed for shipment under

the contract. This clearly excludes a country elevator unless the country elevator is part of a much larger operation that can control shipments of substantial quantities of wheat and feed grains. Consequently, a large vertically integrated business with numerous terminal elevators, sub-terminal elevators and country elevators is in a good position to utilize its volume as a means of reducing freight rates at the country elevator level. This is true even though the country elevator operated by the integrated business is no bigger and has no greater capacity than a competitive country elevator located in the same community which is operating without the benefit of a contract rate.

Section 208(b) of the Staggers Rail Act of 1980 required that the Commission publish special tariff rules for contracts in order to assure that the essential terms of the contracts are available to the general public. In addition, Section 208(d)(2) sets forth certain criteria to be considered by the Commission in approving a contract for the transportation of agricultural commodities and provides that a contract shall not be approved if the rail carrier has unreasonably discriminated against shippers or if the proposed contract constitutes a destructive competitive practice. As a practical matter, these safeguards are of little or no value since none of the detailed information concerning the contract rates is published and available to the general public. A shipper has no information which would be a basis for filing a complaint with respect to any contract rate application. As a practical matter, the only time that the country elevator is aware of the existence of a contract rate is when a competitive elevator consistently offers a slightly higher price to the producers for their commodities, but this does not indicate the extent of the savings available under the contract rate but only to the extent of the savings which are reflected in the market place for the commodities.

We are involved in the storage, handling, merchandising and shipment of wheat and feed grains. We feel that the use of contract rates in connection with the transportation of these commodities has been a significant problem for the small shippers and will reduce or eliminate competition in the market place. We do not know whether or not contract rates are beneficial in connection with the transportation of other products, but with respect to wheat and feed grains we feel that the net effect is to disrupt the existing markets and eliminate the small shipper. We would urge that wheat and feed grains be eliminated in their entirety from the contract rate provisions of the Staggers Rail Act of 1980.

Very truly yours,

S. Dean Evans, Sr., *Partner.*

Union Equity Co-operative Exchange,
Enid, Okla., November 20, 1981.

Hon. Bob Packwood,
Chairman, Commerce, Science and Transportation, U.S. Senate, Dirksen Building, Washington, D.C.

Dear Senator Packwood: This has reference to the oversight hearing held the morning of November 10, 1981, on the Staggers Rail Act of October 14, 1980. It is our understanding that because of the short amount of time allowed at such hearing, and with the need to study this subject thoroughly, your committee has decided to receive written information on this subject during the 60 day period following November 10. We respectfully request that you give consideration to our thoughts and views on the effects of the Staggers Rail Act, which are as follows:

Union Equity does not believe the confidentiality of rail contract rates on bulk grain is in the best interest of either the grain industry or the railroad industry, and such should be deleted from the Staggers Act. We also believe it is wrong to prohibit rail rate bureau activities and unduly prevent railroads from collective rate-making, and the public hearing concept we believe is productive and provides an avenue for indepth discussion by all interested parties of each proposed change in rail freight tariffs. In addition, we do not believe the Staggers Act provides enough time for public notice prior to a given change in a rail rate or other tariff provision. There are times when a rail freight tariff supplement has been in effect for days or weeks before such document is received via U.S. mail, and such lack of ample notice makes it extremely difficult to market grain or any other product.

We respectfully request that you seriously consider amending the Staggers Rail Act of 1980, to remove these most undesirable provisions thereof, and which will better enable us to market grain and conduct our business under this statute.

Yours very truly,

GERALD D. FRAZIER,
Executive Vice President and General Manager.

STATE OF MICHIGAN,
DEPARTMENT OF TRANSPORTATION,
Lansing, Mich., November 23, 1981.

SENATE COMMITTEE ON COMMERCE, SCIENCE AND TRANSPORTATION,
Subcommittee on Surface Transportation, Immigration,
Washington, D.C.
(Attention: Ms. Kathy Meier.)

GENTLEMEN: A major negative effect of the Staggers Rail Act of 1980 on the State of Michigan is the unbearably short time frame in which administrative decisions must be made. Under the 10-day limit in which we may file an offer or an appeal and remain under the protection of the ICC, it is virtually impossible to develop a proper appeal or offer of subsidy. Michigan would like to see the time frames followed for decision making extended to a more reasonable length.

It is our understanding that these comments will be added to the hearing record if received by December 10, 1981.

Sincerely,

JOHN P. WOODFORD, *Director.*

NATIONAL GRANGE,
Washington, D.C., December 1, 1981.

Hon. BOB PACKWOOD,
Chairman, Senate Committee on Commerce, Science and Transportation, Dirksen Senate Office Building, Washington, D.C.

DEAR CHAIRMAN PACKWOOD: The National Grange, like other key members of the agricultural community, is very concerned about rural America's dwindling access to dependable railroad service at affordable rates. This is not a new issue for the Grange. In fact, the bitter struggle of the 1860's between farmers and the railroads spurred the founding of the Grange and the creation of the Grange laws. Grange efforts led to the establishment of the Interstate Commerce Commission to oversee the activities of the nation's railroads. Now, implementation of the Staggers Rail Act has refocused rural America's interest in railroad transportation.

One issue not considered during passage of the railroad deregulation legislation last year is the rail industry's management of its vast natural resource holdings. Many of these holdings are on land granted to the railroads as an inducement to build lines and provide service to remote areas of the country. Now, the carriers have used conglomerate structures to separate the land containing the resources from the rail operations. As the land holdings generate considerable income, this permits the railroads to justify high rate levels under the profit-motivated provisions of the Staggers Act. In many instances, removing the profits generated from the land grants from the rail operations has permitted the railroads to close branch lines in agricultural areas by claiming "inadequacy of income."

The delegates to the National Grange's 115th Annual Meeting held in Spokane, Washington, in November of 1981, adopted the following policy statement on railroad transportation:

"Railroad transportation is essential to the nation, having the power of economic life or death in many rural communities. Agriculture is faced with abandonment of many branch lines by certain railroads who are crying "unprofitable operations," yet these lines appear unprofitable only because they have been separated from the original land grants given to the railroads as an inducement for construction and operation. The land grants are, for the most part, still valuable and profitable, and we believe the railroads should retain their original obligation to continue the operation of these branch lines."

We believe it is time for your committee to conduct hearings on railroad organization and the handling of the land grant resources. We urge particular attention to the central issue of the land grant railroads' obligation to use their land grant income to sustain and strengthen rail operations. The extent to which the carriers have breached their contracts with the government and the people by transferring

land grant assets out of the railroad without adequate compensation should also be examined. Adequate compensation in many areas would be the continuation of rail service to remote areas at reasonable rates. A growing trend toward abandonment of railroad lines could have serious economic repercussions, and must be conscientiously addressed.

The National Grange appreciates the opportunity to comment on this issue important to agriculture and rural America, and we respectfully request the inclusion of our remarks in the hearing record of November 10, 1981.

Sincerely yours,

EDWARD ANDERSEN, *Master.*

NEW ENGLAND POWER, CO.,
Westborough, Mass., December 10, 1981.

Senator JOHN C. DANFORTH,
Chairman, Surface Transportation Subcommittee, Senate Committee on Commerce, Science and Transportation, Russell Senate Office Building, Washington, D.C.

DEAR SENATOR DANFORTH: At your invitation, New England Power Company (NEP) submits its comments on the ICC's implementation of the Staggers Rail Act of 1980. NEP is the generation and transmission subsidiary of New England Electric System, a public utility holding company, whose companies supply electricity to more than one million customers in New England. NEP plans to ship approximately three million tons of coal per year from Appalachian mines to east coast ports, where the coal will be transloaded onto colliers destined for electric generating units in New England.

We support the position of the Edison Electric Institute presented before your Subcommittee at the November 10 hearing. The subsidization of railroads at the expense of the electric utilities' customers must be halted.

NEP has long felt that rail contracts are in the best interest of both coal shipper and railroad. Accordingly, in 1979, when it was clear that its major generating plant would be converted to coal from oil, NEP discussed contracting for rail transportation with the three railroads servicing the relevant mine areas—Consolidated Rail Corporation, The Chessie System, and Norfolk & Western Railway Company. Later, when the Staggers Act was approved, NEP was optimistic about obtaining a contract from carriers, because the Staggers Act clearly permitted enforceable contracts and it reflected a Congressional intent to encourage the use of contracts in railroad transportation.

With the passage of time, however, NEP's optimism has waned substantially. It is now clear that the rate provisions of the Staggers Act—as interpreted by the Interstate Commerce Commission—hold out the likelihood that the railroad will gain such extraordinary profits from their tariff rates on captive coal shipments, that they have no incentive to negotiate contracts for rail transportation of coal. We need only to point to the current status of our contract discussions with the three railroads to document this. While we are in active discussions with both ConRail and N&W, and although drafts have been exchanged, substantial progress beyond that point has yet to be achieved. As to The Chessie System, they have refused to negotiate, obviously anticipating greater profits by not entering into a contract, and relying instead upon their tariff rates. (See attached exchange of letters.) The current good health of these railroads has been reported in the press and admitted in the railroad's own advertisements. (See attachments.) [1]

We propose the following as necessary to promote railroad contracts under the Staggers Act:

1. Amend the Staggers Act to remove existing disincentives for railroads to sign contracts with shippers. For example, the ICC has recently altered the standard for determining whether a railroad possesses "market dominance" such that the ICC can invoke jurisdiction over the railroad's rates. The ICC has made product and geographic competition relevant factors in determining market dominance with the effect that it may be virtually impossible for a shipper to obtain a determination of the reasonableness of a railroad tariff rate. We urge action to compel reversion to prior standards, which do not permit the misleading factors of product and geographic competition to rebut the true measure of market dominance—excess railroad profits. Failure to revert to this standard has the potential of bestowing on railroads unbridled discretion to raise their tariffs, thereby making such railroads unreceptive to shippers' overtures for railroad contracts;

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[1] Attachments referred to have been retained in committee files.

2. Amend the Staggers Act to provide positive incentives to those railroads that do sign contracts with shippers. For example, Congressional action along the lines of requiring a fixed percentage of railroad revenues from tariffs to be devoted to capital additions, with a smaller percentage of revenues from contracts to be devoted to capital additions, will provide the necessary positive incentive to railroads to negotiate contracts with shippers;

3. Require the ICC to comply with the spirit and underlying basis of the Staggers Act in its implementation. It is necessary to curb the ICC's pre-disposition in favor of the railroads in critical rulemakings, to date exhibited by ICC actions unfairly impacting shippers. For example, ICC rulings in Ex Parte 290 (Inflationary Cost Increases), Ex Parte 320 (Market Dominance), and Ex Parte 393 (Railroad Revenue Adequacy) ignore the Congressional intent expressed in enacting the Staggers Act.

We hope the Committee will consider these necessary actions to encourage the railroads to enter into contracts with shippers, and thereby make the Staggers Act work as originally intended.

We thank you for the opportunity to comment on the Staggers Act.

Very truly yours,

PASCO GASBARRO, Jr.,
Assistant General Counsel.

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